Section 1

Employee Retirement System
Summary of Recommendations - Senate

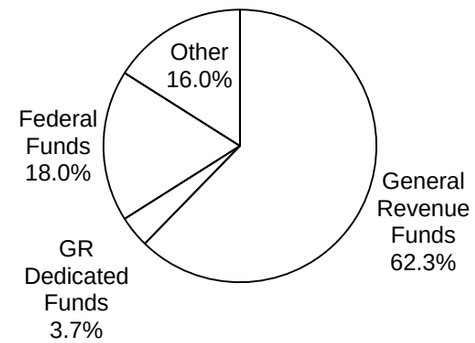
Page: I-36
Paula Jones, Acting Executive Director

Emily Morganti, LBB Analyst

Method of Financing	2012-13 Base	2014-15 Recommended	Biennial Change	% Change
General Revenue Funds	$2,114,512,744	$2,461,562,600	$347,049,856	16.4%
GR Dedicated Funds	$127,694,381	$147,952,706	$20,258,325	15.9%
Total GR-Related Funds	*$2,242,207,125*	*$2,609,515,306*	*$367,308,181*	*16.4%*
Federal Funds	$635,001,773	$709,760,759	$74,758,986	11.8%
Other	$532,074,559	$632,847,750	$100,773,191	18.9%
All Funds	**$3,409,283,457**	**$3,952,123,815**	**$542,840,358**	**15.9%**

	FY 2013 Budgeted	FY 2015 Recommended	Biennial Change	% Change
FTEs	0.0	0.0	0.0	0.0%

RECOMMENDED FUNDING
BY METHOD OF FINANCING



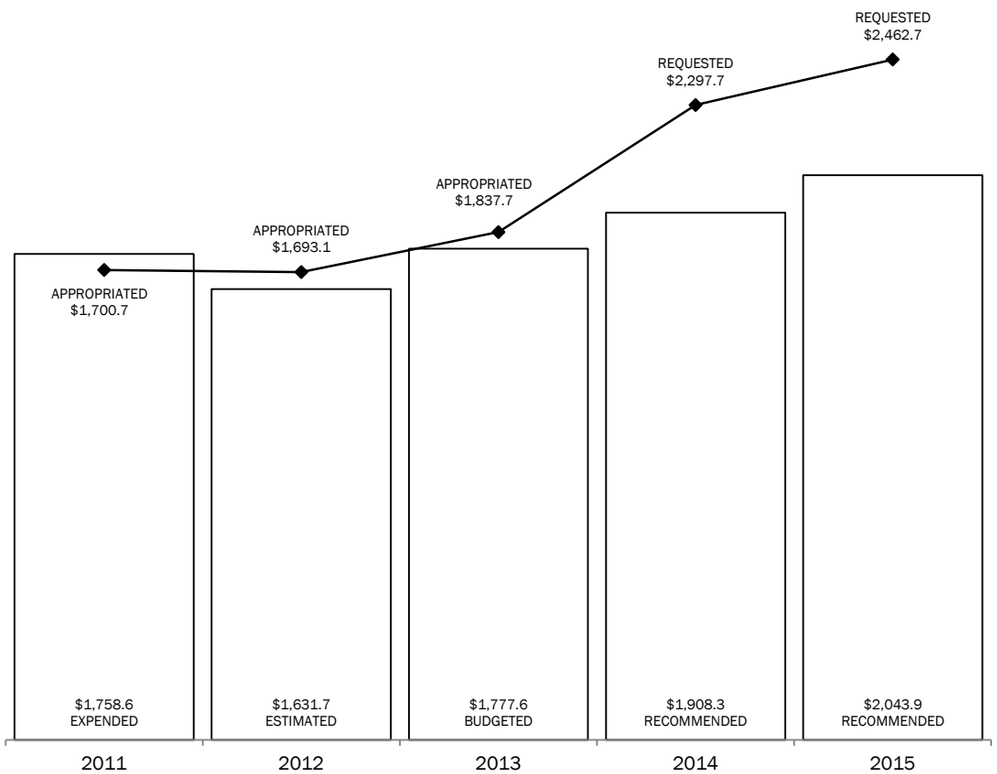
The bill pattern for this agency (2014-15 Recommended) represents an estimated 10.5% of the agency's estimated total available funds for the 2014-15 biennium.

Section 1
Employees Retirement System

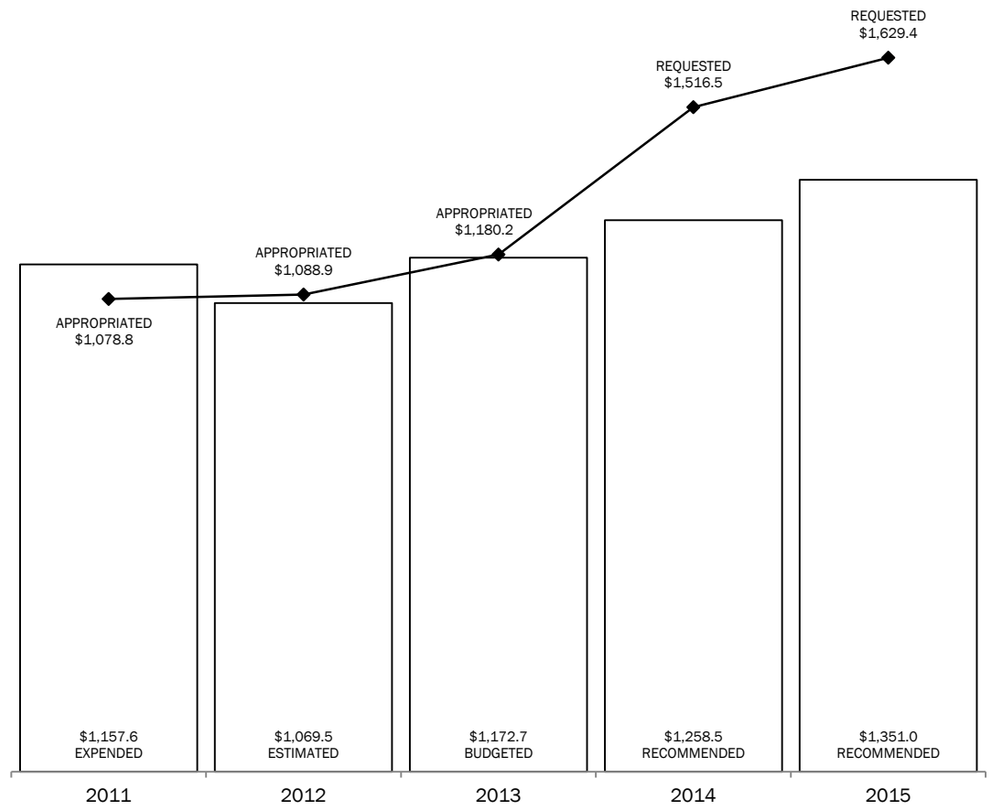
2014-2015 BIENNIUM TOTAL= $3,952.2 MILLION

IN MILLIONS

ALL FUNDS



GENERAL REVENUE AND GENERAL REVENUE-DEDICATED FUNDS



Section 2

Employee Retirement System
Summary of Recommendations - Senate, By Method of Finance -- ALL FUNDS

Strategy/Goal	2012-13 Base	2014-15 Recommended	Biennial Change	% Change	Comments
RETIREMENT CONTRIBUTIONS A.1.1	$711,380,320	$743,611,437	$32,231,117	4.5%	Recommendations reflect an All Funds increase of $32.2 million above 2012-13 funding levels for the state's contribution of 6.5 percent of payroll in each fiscal year of the 2014-15 biennium to the retirement system for general state employees, which is a biennialization of the fiscal year 2013 contribution rate. Recommendations assume no annual payroll growth and reflect projected significant changes in the number of FTEs and/or funding of FTEs at certain state agencies (See Selected and Fiscal and Policy Issues #2).
LECOS A.1.2	$7,520,372	$15,040,744	$7,520,372	100.0%	Recommendations reflect an All Funds increase of $7.5 million above 2012-13 funding levels for the state's contribution of 0.5 percent of payroll in each fiscal year of the 2014-15 biennium to the LECOS retirement system. This is an increase over the 2012-13 contribution rate of 0.0 percent (See Selected Fiscal and Policy Issues #3).
JRS-II A.1.3	$8,537,894	$8,779,486	$241,592	2.8%	Recommendations reflect an All Funds increase of $0.2 million above 2012-13 funding levels for the state's contribution of 6.5 percent of payroll in each fiscal year of the 2014-15 biennium to the Judicial Retirement System – Plan 2 for a biennialization of the fiscal year 2013 contribution rate. (See Selected Fiscal and Policy Issues #4).
JRS-I A.1.4	$53,132,972	$53,132,972	$0	0.0%	Recommendations assume no growth over 2012-13 spending levels to pay for benefits of retirees in the Judicial Retirement System – Plan 1, which is operated on a pay-as-you-go basis. JRS-1 participants are those retired judges who joined the bench prior to 1985.
PUBLIC SAFETY BENEFITS A.1.5	$10,943,701	$10,943,701	$0	0.0%	Recommendations assume no growth over 2012-13 spending levels for benefit payments to the survivors of public law enforcement or fire fighting personnel who are killed in the line of duty.
RETIREE DEATH BENEFITS A.1.6	$16,748,964	$16,748,964	$0	0.0%	Recommendations assume no growth over 2012-13 spending levels for lump sum death benefit payments to the survivors or estate of a person retired under any of the ERS-administered programs.
Total, Goal A, EMPLOYEES RETIREMENT SYSTEM	**$808,264,223**	**$848,257,304**	**$39,993,081**	**4.9%**	

Section 2

Employee Retirement System
Summary of Recommendations - Senate, By Method of Finance -- ALL FUNDS

Strategy/Goal	2012-13 Base	2014-15 Recommended	Biennial Change	% Change	Comments
GROUP INSURANCE B.1.1	$2,601,019,234	$3,103,866,511	$502,847,277	19.3%	Recommendations provide for an All Funds increase of $502.8 million over 2012-13 spending levels for a state contribution rate increase of 7.36 (net) percent in fiscal year 2014 and 7.33 (net) percent in fiscal year 2015. The contribution rate increase for each fiscal year of the biennium is based on: • Actual and projected expenditures for the previous fiscal year; • Funding a 7.0 percent benefit cost trend; spending down between $157.6 million and $177.6 million of the ERS-projected insurance fund balance over the biennium; and • The 1.0 percent contribution of payroll by state agencies and institutions of higher education assuming no payroll growth. Recommendations also provide for 5 percent annual growth in retirees, resulting in approximately 1.5 percent growth in overall total population per fiscal year, as well as projected changes in the number and/or funding of FTEs at certain state agencies (See Selected Fiscal and Policy Issue #1).
Total, Goal B, EMPLOYEES RETIREMENT SYSTEM	**$2,601,019,234**	**$3,103,866,511**	**$502,847,277**	**19.3%**	
Grand Total, All Strategies	**$3,409,283,457**	**$3,952,123,815**	**$542,840,358**	**15.9%**	

Section 2

Employee Retirement System
Summary of Recommendations - Senate, By Method of Finance -- GENERAL REVENUE FUNDS

Strategy/Goal	2012-13 Base	2014-15 Recommended	Biennial Change	% Change	Comments
RETIREMENT CONTRIBUTIONS A.1.1	$425,580,676	$445,295,015	$19,714,339	4.6%	Recommendations reflect an increase of $19.7 million in General Revenue above 2012-13 funding levels for the state's contribution of 6.5 percent of payroll in each fiscal year of the 2014-15 biennium to the retirement system for general state employees. Recommendations assume no payroll growth in either year of the biennium and reflect projected significant changes in the number and/or funding of FTEs at certain state agencies.
LECOS A.1.2	$6,698,395	$13,396,790	$6,698,395	100.0%	Recommendations reflect an increase of $6.7 million in General Revenue above 2012-13 funding levels for the state's contribution of 0.5 percent of payroll in each fiscal year of the 2014-15 biennium to the LECOS retirement system.
JRS-II A.1.3	$5,122,737	$5,267,692	$144,955	2.8%	Recommendations reflect an increase of approximately $0.1 million in General Revenue above 2012-13 funding levels for the state's contribution of 6.5 percent of payroll in each fiscal year of the 2014-15 biennium to the Judicial Retirement System – Plan 2 (JRS-II).
JRS-I A.1.4	$53,132,972	$53,132,972	$0	0.0%	Recommendations assume no growth over 2012-13 spending levels to bay for benefits of retirees in the Judicial Retirement System – Plan 1 (JRS-I), which operates on a pay-as-you-go plan. JRS-I participants are those retired judges who joined the bench prior to 1985.
PUBLIC SAFETY BENEFITS A.1.5	$7,568,701	$7,551,053	($17,648)	(0.2%)	Recommendations assume no growth over the 2012-13 spending levels for benefit payments to the survivors of public law enforcement or fire fighting personnel who are killed in the line of duty.
RETIREE DEATH BENEFITS A.1.6	$16,748,964	$16,748,964	$0	0.0%	Recommendations assume no growth over 2012-13 spending levels for lump sum death benefit payments to the survivor or estate of a person retired under any of the ERS-administered programs.
Total, Goal A, EMPLOYEES RETIREMENT SYSTEM	**$514,852,445**	**$541,392,486**	**$26,540,041**	**5.2%**	

Section 2

Employee Retirement System

Summary of Recommendations - Senate, By Method of Finance -- GENERAL REVENUE FUNDS

Strategy/Goal	2012-13 Base	2014-15 Recommended	Biennial Change	% Change	Comments
GROUP INSURANCE B.1.1	$1,599,660,299	$1,920,170,114	$320,509,815	20.0%	Recommendations provide for a General Revenue increase of $320.5 million over 2012-13 spending levels for a state contribution rate increase of 7.36 (net) percent in fiscal year 2014 and 7.33 (net) percent in fiscal year 2015. The contribution rate increase for each fiscal year of the biennium is based on: • Actual and projected expenditures for the previous fiscal year; • Funding a 7.0 percent benefit cost trend; spending down between $157.6 million and $177.6 million of the ERS-projected insurance fund balance over the biennium; and • The 1.0 percent contribution of payroll by state agencies and institutions of higher education assuming no payroll growth. Recommendations also provide for 5 percent annual growth in retirees, resulting in approximately 1.5 percent growth in overall total population per fiscal year, as well as projected changes in the number and/or funding of FTEs at certain state agencies (See Selected Fiscal and Policy Issue #1).
Total, Goal B, EMPLOYEES RETIREMENT SYSTEM	**$1,599,660,299**	**$1,920,170,114**	**$320,509,815**	**20.0%**	
Grand Total, All Strategies	**$2,114,512,744**	**$2,461,562,600**	**$347,049,856**	**16.4%**	

Section 2

Employee Retirement System

Summary of Recommendations - Senate, By Method of Finance -- 6 - State Highway Fund

Strategy/Goal	2012-13 Base	2014-15 Recommended	Biennial Change	% Change	Comments
RETIREMENT CONTRIBUTIONS A.1.1	$115,891,040	$124,694,298	$8,803,258	7.6%	Recommendations reflect an increase of $8.8 million in State Highway Fund No. 006 above 2012-13 funding levels for the state's contribution of 6.5 percent of payroll each fiscal year of the 2014-15 biennium to the retirement system for certain general state employees.
LECOS A.1.2	$696,386	$1,392,772	$696,386	100.0%	Recommendations reflect an increase of $0.7 million over 2012-13 funding levels for the state's contribution of 0.5 percent of payroll each fiscal year of the 2014-15 biennium to the LECOS retirement system.
JRS-II A.1.3	$0	$0	$0	0.0%	
JRS-I A.1.4	$0	$0	$0	0.0%	
PUBLIC SAFETY BENEFITS A.1.5	$0	$0	$0	0.0%	
RETIREE DEATH BENEFITS A.1.6	$0	$0	$0	0.0%	
Total, Goal A, EMPLOYEES RETIREMENT SYSTEM	**$116,587,426**	**$126,087,070**	**$9,499,644**	**8.1%**	
GROUP INSURANCE B.1.1	$396,615,080	$485,542,920	$88,927,840	22.4%	Recommendations provide for an increase of $88.9 million over 2012-13 spending levels. Recommendations provide for a state contribution rate increase of 7.36 percent (net) in FY 2014 and 7.33 percent in FY 2015.
Total, Goal B, EMPLOYEES RETIREMENT SYSTEM	**$396,615,080**	**$485,542,920**	**$88,927,840**	**22.4%**	
Grand Total, All Strategies	**$513,202,506**	**$611,629,990**	**$98,427,484**	**19.2%**	

Employees Retirement System
Selected Fiscal and Policy Issues

1. **Group Benefits Program.** Recommendations reflect an increase of $320.5 million in General Revenue and $502.8 million in All Funds above 2012-13 spending levels.

   Contribution Increases. ERS requested a state contribution increase of 8.0 percent in fiscal year 2014 and an increase of 8.0 percent in fiscal year 2015. This request assumes use of $148.5 million (state agency portion is $83.9 million) from the GBP contingency reserve as of the end of fiscal year 2013. The recommendations provide for a state contribution rate increase of 7.36 percent in fiscal year 2014 and 7.33 percent in fiscal year 2015 and assumes spending down between $157.6 million and $177.6 million of the ERS-projected insurance fund balance as of August 31, 2013. Recommendations provide for 5.0 percent annual growth in retirees, resulting in approximately 1.5 percent growth in overall total population per fiscal year. The recommendations fund an annual benefits cost trend of 7.0 percent in each fiscal year. In addition, state agencies also contribute 1 percent of payroll to help cover a total 8.0 percent projected annual growth in healthcare claims.

   Assumptions. The agency's request assumes no growth in retirees or FTE's in FY 2014 and 0.77 percent enrollment growth is assumed in fiscal year 2015 related to the change in waiting period required by the by federal healthcare reform. This differs from the assumptions mentioned above.

2. **ERS Retirement Program.** Recommendations reflect an increase of $19.0 million in General Revenue and $32.2 million in All Funds above 2012-13 funding levels.

   Retirement Rates. The following summarizes the rates for recommended and requested amounts as well as constitutional and statutory requirements, as of the August 31, 2012 valuation of the Employees Retirement System. The agency's base request assumes a state contribution rate of 6.5 percent. The state contribution rate decreased from 6.95 percent to 6.0 percent on September 1, 2011 and increased to 6.5 percent on September 1, 2012.

   Recommended and Requested Contribution Rates for ERS Retirement
   - 6.5 percent – Recommended State Contribution Rate (sustains current rate)
   - 10.0 percent – Requested state contribution rate (up to constitutional maximum)
   - 11.75 – Actuarially sound state contribution rate

   Constitutional/Statutory Contribution Rates for ERS Retirement
   - 6.0 percent – Constitutional minimum state contribution rate
   - 7.4 percent – Statutorily required state contribution rate, Government Code Section 815.403
   - 10.0 percent – Constitutional maximum state contribution rate

   Assumptions. The agency's request assumes no growth in salaries or FTEs, which differs from the following assumptions, which include a 0.0 percent growth in salaries but does assume projected FTE changes at certain state agencies during the 2014-15 biennium. These include the

FTE additions at the Department of Transportation, the Office of the Attorney General, the Texas Education Agency, and the Texas Facilities Commission. These increases are partially offset by an FTE reduction at the Texas Workforce Commission. Please note that funding levels for retirement may be adjusted based on the salary and FTE impact of the overall recommendations.

Actuarial Status. According to the August 31, 2012 actuarial valuation of the ERS Retirement Fund, its actuarial value of assets is approximately $24.3 billion, an increase of $0.3 billion from valuation completed one year earlier. The plan's funded ratio is 81.0 percent, which is lower than the plan's 82.6 percent funded ratio one year earlier. The February 28, 2013 updated of the ERS Retirement fund valuation is expected to be available in mid-March, 2013.

3. **Law Enforcement and Custodial Officer Supplemental (LECOS) Retirement Program**

LECOS Retirement Fund Contribution Rates. The following summarizes the rates for state contributions, as well as requested contribution percentages as of August 31, 2012 actuarial valuation of the LECOS retirement fund. The agency's base request assumes a state contribution rate of 0.5 percent. The state contribution rate decreased from 1.59 percent to 0.0 percent on September 1, 2011 and increased to 0.5 percent on September 1, 2012.

Recommended and Requested Contribution Rates for LECOS

- 0.5 percent – Recommended state contribution rate (sustains current rate)
- 2.07 percent – Requested actuarially sound state contribution rate

Actuarial Status. According to the August 31, 2012 actuarial valuation of the LECOS Retirement Fund, its actuarial value of assets is approximately $832.5 million, an increase of $1.9 million from the valuation completed on year earlier. The plan's funded ratio is 79.7 percent, which is lower than the plan's 83.7 percent funded ratio one year earlier. The February 28, 2013 updated of the ERS Retirement fund valuation is expected to be available in mid-March, 2013. Senate Bill 1664, Eighty-second Legislature, amended Government Code Section 815.317 to redirect certain local criminal court fees to the LECOS Retirement Fund beginning September 1, 2013. ERS indicated that the actuarial valuation will begin reflecting this new revenue source in fiscal year 2014.

4. **Judicial Retirement System – Plan Two (JRS II)**

JRS II Contribution Rates. The following summarizes the rates for state contributions, as well as requested contribution percentages as of the August 31, 2012 actuarial valuation of the JRS II fund. The agency's base request assumes a state contribution rate of 6.5 percent. The state contribution rate decreased from 16.83 percent to 6.0 percent on September 1, 2011 and increased to 6.5 percent on September 1, 2012.

Recommended and Requested Contribution Rates for JRS II

- 6.5 percent – Recommended state contribution rate (sustains current rate)
- 15.76 percent – Requested actuarially sound state contribution rate

Actuarial Status. According to the August 31, 2012 actuarial valuation of the JRS-II Fund, its actuarial value of assets is approximately $300.4

million, an increase of $16.5 million from the valuation completed on year earlier. The plan's funded ratio is 95.3 percent, which is higher than the plan's 94.6 percent funded ratio one year earlier. The February 28, 2013 updated of the ERS Retirement fund valuation is expected to be available in mid-March, 2013.

5. **Federal Healthcare Legislation.** On March 23, 2010, the Patient Protection and Affordable Care Act was signed into law. Study of this legislation indicates that the Group Benefits Program (GBP) will be affected in the 2014-15 biennium by different provisions of the legislation. These effects are summarized below:

   - **Coverage of preventative services** (Effective September 1, 2011) – Eliminating the cost-sharing (co-pays, deductibles, and coinsurance) for preventative services. ERS estimates that this will result in an additional cost of $14 million in All Funds during the 2014-15 biennium.
   - **Dependent coverage** (Effective September 1, 2011) – Provide dependent coverage for dependents up to age 26. Prior to this taking effect, GBP provides coverage for dependents up to age 25. ERS estimates this provision will result in costs of $3 million in All Funds during the 2014-15 biennium.
   - **Reduced waiting period** (September 1, 2014) – The waiting period for new employees to receive health insurance is reduced to 90 days beginning in fiscal year 2015. ERS estimates this will result in costs of $15 million in All Funds during the 2014-15 biennium.
   - **Transitional Reinsurance Fee** – Fee assessed on plans to help stabilize the health insurance market when health insurance exchanges become operational. The fee will be effective in fiscal year 2014 and will continue through fiscal year 2016. ERS estimates that this will result in additional costs of $35.3 million in All Funds during the 2014-15 biennium.

   Recommendations account for costs and savings related to the Affordable Care Act.

6. **Senate Bill 1664, Eighty-Second Legislature, Regular Session, 2011.** Senate Bill 1664 amended Government Code Section 815.317 to redirect 11.14 percent of certain local criminal court fees to the Law Enforcement and Custodial Officer Supplemental retirement fund instead of the Chauffeur's License Fund beginning September 1, 2013. This new revenue source, estimated to be $21.3 million in each fiscal year, will have no effect on the member or employer contribution rates, but is expected to offset the unfunded liability of the fund.

   Senate Bill 1664 also amended Insurance Code Section 1551.3075 to require all employees, retirees, and dependents who use tobacco to pay an additional $30 to $90 per month for their health insurance, depending on how many tobacco users in their families are covered by the plan. The fee offsets additional health costs associated with tobacco use, as well as provides an incentive for users to quit. According to the Comptroller's Cash Report for fiscal year 2012, the agency collected approximately $4.3 million in fiscal year 2012. The agency projects an estimated $8.8 million will be collected in fiscal year 2013 from this fee. Additionally, the agency projects an estimated $7.6 million fiscal year 2014 and $8.0 million in fiscal year 2015 will be collected from this fee, and these amounts are reflected in Rider 11 of the agency's bill pattern. The agency indicated that they plan to switch from the current opt-in structure to an opt-out structure for tobacco user certification and expect to collect additional revenue from this change.

7. **Payroll Contribution for Group Health Insurance.** In the 2012-13 General Appropriations Act, Article IX, Section 18.09 directs all agencies and institutions of higher education to contribute an amount totaling 1.0 percent of total base wages and salaries to the ERS to offset benefit costs within the GBP. During fiscal year 2012, ERS received approximately $54.9 million in All Funds from state agencies, and approximately $31.6

million in All Funds from institutions of higher education. ERS expects to receive approximately $87.1 million in All Funds from agencies and institutions of higher education in fiscal year 2013. Recommendations maintain the 1.0 percent of payroll contribution to ERS. Based on the assumption of no payroll growth for state agencies and 2 percent growth for institutions of higher education, it is estimated that ERS will receive approximately $176.2 million in All Funds from agencies and institutions of higher education for the 1.0 percent contribution in the 2014-15 biennium.

8. **Analysis of the Benefits Cost Trend and Insurance Reserve Fund.** Figures 1 and 2 on the following pages show the history of the GBP's benefit cost trend, as well as the history of the state contribution increases to ERS for health insurance. Figure 3 shows the history of the GBP contingency fund balance.

The Texas Employees Group Benefits Program (GBP) is the group health benefits program for state and higher education (excluding the Texas A&M University and University of Texas systems) employees, retirees, and their dependents. The state funds 100 percent of the monthly premium for full-time employees and 50 percent of dependent coverage, with members paying the other 50 percent of the dependent coverage. Active employees who work part-time receive a state contribution which is 50 percent of the rate of full-time employees for health insurance.

One of the major cost drivers for the GBP is the benefit cost trend, which is the rate at which GBP health benefits costs are increasing annually. There are three components of the benefit cost trend: hospital costs, prescription drug costs, and other medical expenses.

The data in the following figures shows three bar graphs for each fiscal year dating back to fiscal year 2004. Figure 1 represents a ten year history of the benefit cost trend. The first bar for each fiscal year reflects the benefit cost trend that the Employees Retirement System (ERS) assumed for that fiscal year in its Legislative Appropriations Request (LAR) for that particular biennium. The second bar reflects an updated benefit cost trend assumption that was submitted by ERS at the beginning of the legislative session for that particular biennium. Finally, the third bar reflects the actual benefit cost trend, based on actual claims expenditures through the end of the following fiscal year.

In Figure 1, the negative benefit cost trend bars in fiscal year 2004 reflected the anticipated and realized, respectively, savings from the benefit reductions that were implemented May 1, 2003 by the ERS Board of Trustees, and September 1, 2003, by the Legislature in order to address the state's budgetary constraints during that time period. These benefit reductions, as well as other cost savings measures which ERS implemented, including reduction in the reimbursement rates applicable to mail service prescription drugs, mitigated benefit cost trend increases in fiscal years 2005 and 2006. The benefit cost trend was further mitigated in fiscal year 2007 due to a renegotiation of the Pharmacy Benefits Manager (PBM) contract as a result of the "Most Favored Nations" provision in the contract, which requires the PBM to give ERS its most favorable contract terms. In fiscal year 2010, the benefit cost trend was reduced as a result of a settlement involving the Average Wholesale Price (AWP) structure for pharmaceutical drugs. The benefit cost trend was significantly reduced in fiscal year 2011 as a result of benefit changes made by the ERS Board of Trustees due to budgetary constraints, as well as changes to the PBM contract. The benefit cost trend figures for fiscal years 2012 and 2013 are ERS' projections for the rest of the biennium, as of August 2012.

Figure 2 represents a ten year history of the increases in the per capita state contribution rate for the GBP. The per capita state contribution rate for the GBP reflects how much the plan must contribute for each participant monthly to cover health claims costs. The first bar for each fiscal year reflects the increase in the state contribution rate benefit cost trend that ERS requested for that fiscal year in its LAR for that biennium. The

second bar reflects an updated request for a state contribution increase that was submitted by ERS at the beginning of the legislative session for that biennium. Finally, the third bar reflects the actual state contribution increase, or decrease, appropriated by the Legislature for that particular fiscal year.

In Figure 2, the negative state contribution rate shown in fiscal year 2004 reflected the appropriation reductions made by the Legislature in order to address the state's budgetary constraints during that time period. The state contribution increases in the 2006-07 biennium were less than the projected 12 percent cost trend in order to account for continued savings resulting from the benefits revisions made in the previous biennium. In the 2008-09 biennium, the state contribution increased minimally from the previous biennium due to the Legislature's directive to ERS to spend down the insurance contingency reserve fund balance, which was higher than projected at the end of fiscal year 2007 due to lower than anticipated utilization, greater than expected investment income, and the continued residual effect on cost containment efforts implemented in fiscal year 2003. The contingency reserve fund, established by Insurance Code, Section 1551.211, receives all revenues for the GBP, including state and member contributions, federal subsidies, prescription drug rebates, and investment income, and makes expenditures to cover GBP-related claims costs. For the 2010-11 biennium, the Legislature appropriated a state contribution increase that was supplemented with the insurance contingency reserve fund balance to meet the projected benefit cost trend. However, due to a higher than projected cost trend in fiscal year 2011, the ERS Board of Trustees made benefit revisions in order to ensure adequate GBP funding through the 2010-11 biennium. The state contribution rate increases shown for the 2012-13 biennium reflect both direct GBP appropriations for ERS, as well as revenue from Article IX, Section 18.09, Payroll Contributions for Group Health Insurance, 2012-13 General Appropriations Act. This provision required all participating entities in the GBP to contribute one percent of its total base wages and salaries for each benefits eligible employee to the GBP.

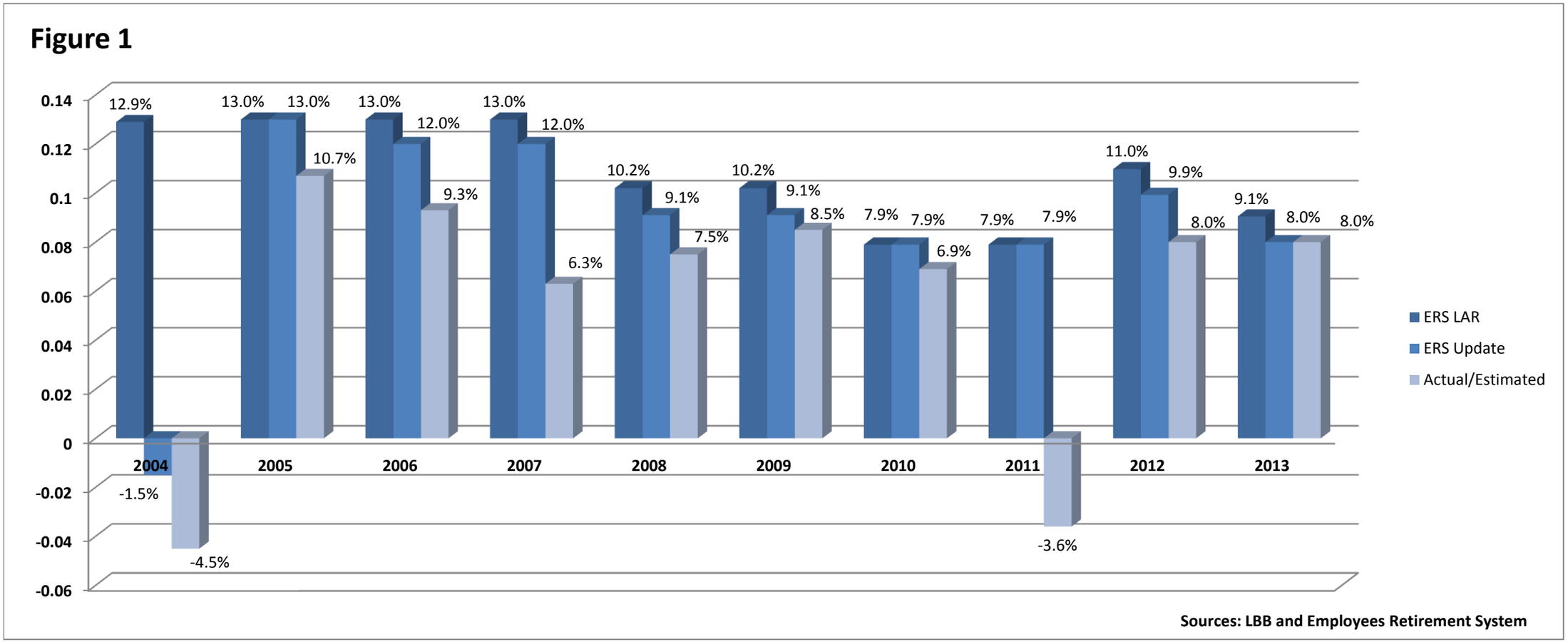
Figure 3 represents a ten year history of the contingency fund balance as of the end of the fiscal year. The increases in fund balance in fiscal years 2011 and 2012 are primarily related to additional federal funding from the Early Retiree Reinsurance Program (ERRP), an initiative of the Affordable Care Act, to offset costs associated with covering retirees not yet eligible for Medicare.

9. **Growth Assumptions for Other State Funded Retirement and Insurance Programs.** Attachment A provides a summary of growth assumptions and state contribution rates for the 2014-15 biennium for all state funded retirement and insurance programs.

10. **Retirement Program Study.** Article IX, Section 18.03, Pension Plan Changes Study, in the 2012-13 GAA required the agency to conduct a sustainability study of the ERS Retirement program. Attachment B provides a summary of the findings and options identified by ERS.

11. **Insurance Program Study.** Rider 13, Group Insurance Program Study, in the agency’s bill pattern in the 2012-13 GAA required ERS to conduct a sustainability study of the ERS Insurance program. Attachment C provides a summary of the findings and options identified by ERS.

HealthSelect Benefit Cost Trend



Increase in Per Capita State Contribution Rate

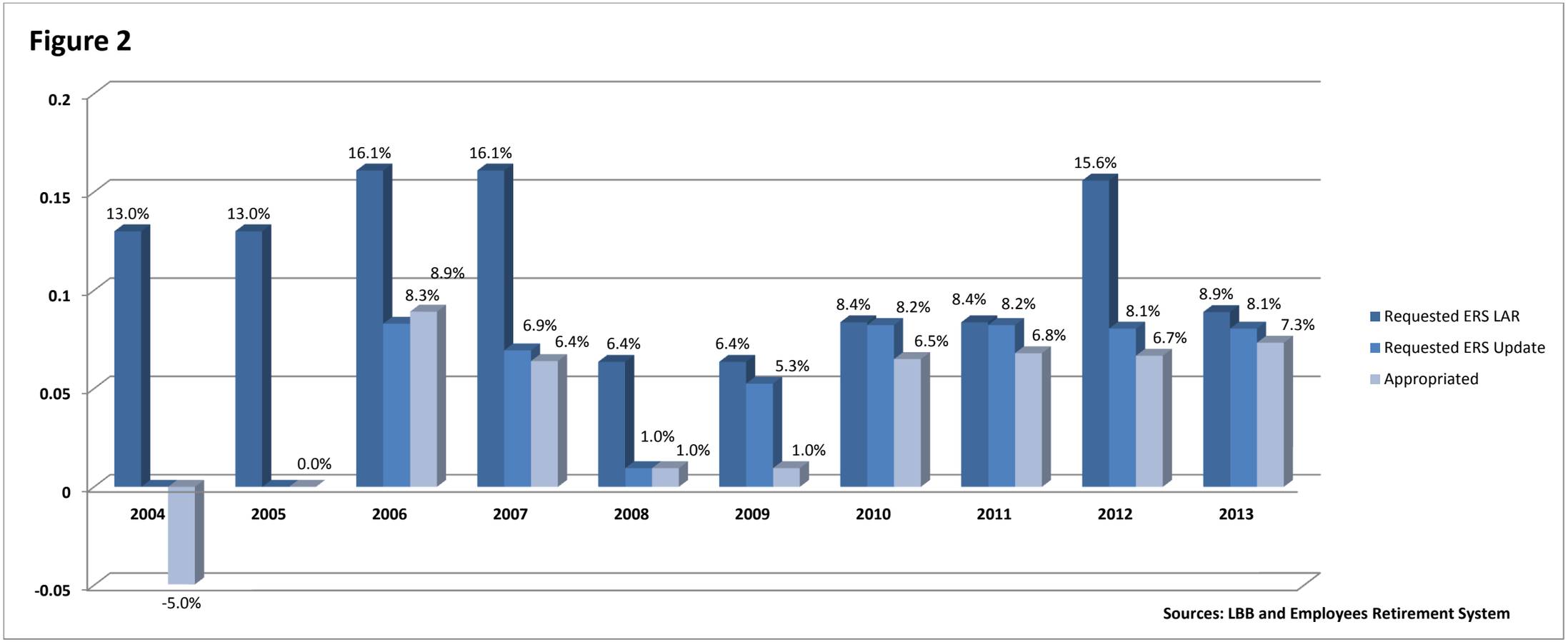
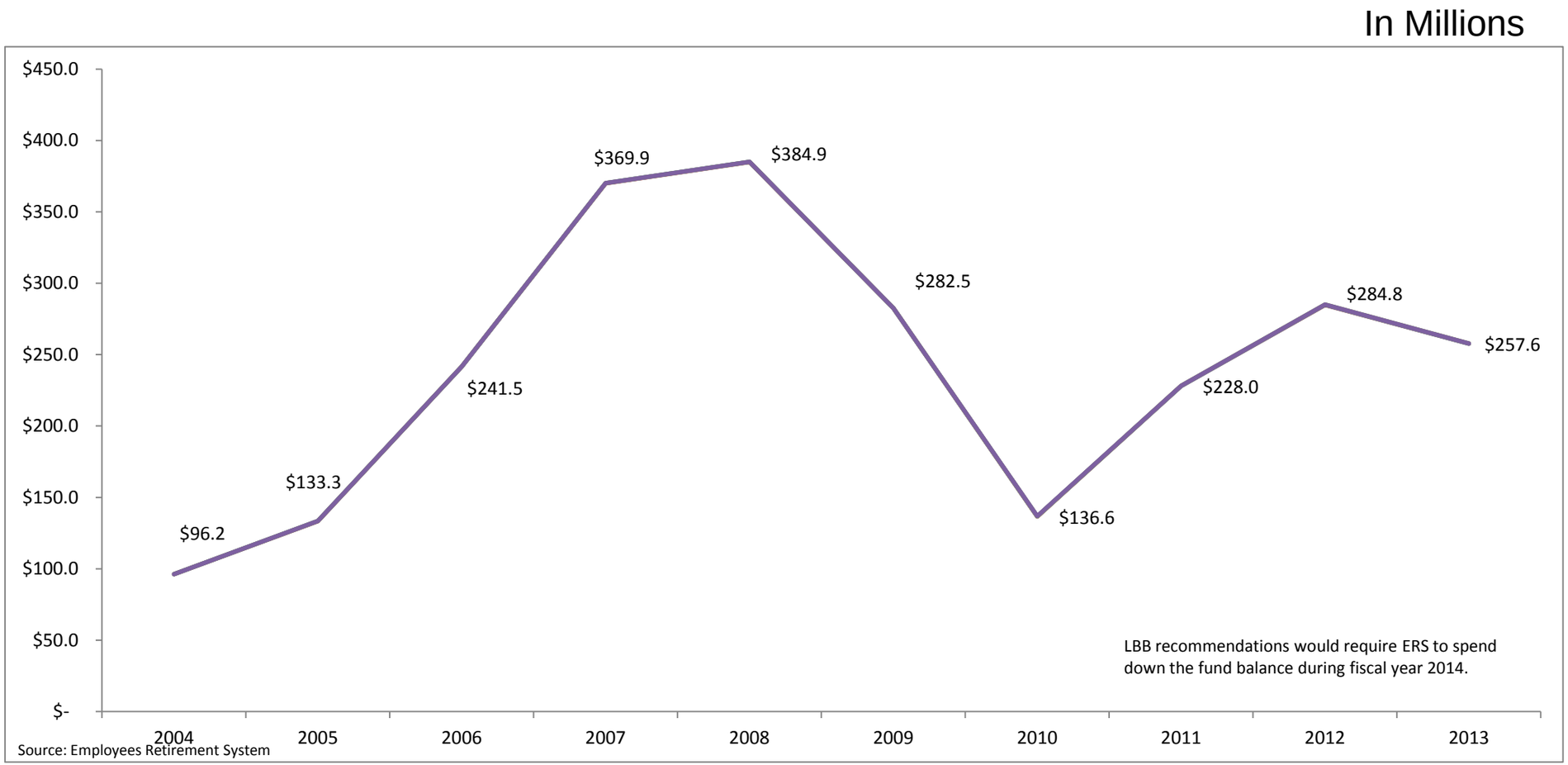


Figure 3

Contingency Reserve Fund Balance



Source: Employees Retirement System

Growth Assumptions and State Contribution Rates for 2014-15

RETIREMENT	2014	2015
Payroll Growth		
Employees Retirement System	0.0%	0.0%
Teacher Retirement System		
Public Education	0.0%	0.0%
Higher Education	2.0%	2.0%
TRS-Care Retiree Insurance	0.0%	0.0%
State Contribution		
Employees Retirement System		
Retirement	6.5%	6.5%
LECOS	0.5%	0.5%
JRS II	6.5%	6.5%
Teacher Retirement System		
Public Education	6.4%	6.4%
Higher Education	6.4%	6.4%
TRS-Care Retiree Insurance	1.0%	1.0%

INSURANCE	2014	2015
Retiree Growth		
Employees Retirement System	5.0%	5.0%
Teacher Retirement System		
Public Education	6.0%	6.0%
Higher Education	6.0%	6.0%
TRS-Care Retiree Insurance	6.0%	6.0%
Active/Retiree Headcount Growth		
Higher Education Group Insurance		
UT Institutions, TAMU Institutions/Agencies, & ERS Institutions of Higher Education	5.04%	5.04%
Community Colleges	0.01%	0.01%
Benefit Cost Growth		
Employees Retirement System	8.0%	8.0%
Teacher Retirement System	N/A	N/A

Employees Retirement System (ERS)
Retirement Program Report

ERS administers the state-supported defined benefit (DB) pension plan for retired state employees. The 2012-13 General Appropriations Act, Article IX, Section 18.03 required the agency to conduct a long-term sustainability study that reviewed plan design changes, including changes within the existing defined benefit plan and hybrid plan alternatives. This study is the result of a 2011 GEER report recommendation on pension solvency. The agency reported eight findings and 14 options, including hybrid and defined contribution (DC) plans.

Report Findings:

1. Unfunded liability will continue to increase without action.
2. A balance of options can be used to make the current plan sound.
3. Establishing an alternative plan could fulfill workforce needs but it does not erase existing DB plan liabilities, and may cost more.
4. Prefunded pooled investing increases value to members and the State.
5. Retirement benefits are critical in attracting and retaining qualified employees.
6. It is difficult to make direct comparisons between the private and public sectors.
7. Changes to other parts of the employee compensation package can impact the retirement plan.
8. Any plan modification or structural change carries legal risks that increase as more members are included.

Options for Solvency Included in the Report:

PLAN OPTION	DESCRIPTION	FISCAL AND ACTUARIAL IMPACT DETAILS
Section 3: Increase Revenues		
3.1 Increase Contribution Rates	Increase the total contribution rate to the trust fund by increasing the state contribution, the employee contribution, or both. Rate increases could be fixed or variable to ensure coverage of all costs.	To reach actuarial soundness, the total contribution rate would have to increase by 4.47%, or $259 million, per year, based on the FY 2011 valuation.
3.2 Pension Obligation Bonds	Issue a General Obligation (GO) or state bond with repayment funded by a consistent source owned by the state.	Depends upon the amount of bonds issued. Bonds can be used to pay all or a portion of unfunded liability.
3.3 Use one-time revenue source	Make a one-time payment for the full amount or some other amount to pay off all or a portion of the unfunded liability.	Depends upon the amount of the one-time contribution. It can be used to pay all or a portion of unfunded liability
3.4 Use alternate, ongoing funding source	Direct lapsed GR dollars into fund or use a dedicated revenue source similar to the criminal court fee revenue provided to LECOSRF.	Depends upon the amount of dedicated revenue or lapse.
Section 4: Modify Plan Design[1]		
4.1 Change Final Average Salary Calculation to 60 Months	Bases the final average salary calculation used to determine benefit amounts on the highest average salary for over 60 months for affected employees.	Reduces unfunded liability by an estimated $216.0 million for high impact/high risk grandfathering.

4.2 Eliminate Use of Unused Leave	Eliminates ability to use sick and annual leave balances to increase service time or increase annuity benefits.	Reduces unfunded liability by an estimated $183.0 million for high impact/high risk grandfathering.
4.3 Reduce Benefit Multiplier for Future Service and Allow Employees to "Buy Up" to Increase Their Multiplier	Reduces the multiplier for future service from 2.3% to 2% for non-grandfathered employees. Allows affected employees to pay an increased contribution rate to "buy up" their multiplier to the 2.3% level at the actuarial cost.	Reduces unfunded liability by an estimated $375.0 million for high impact/high risk grandfathering.
4.4 Apply September 1, 2009 Changes to All Employees	Applies the benefit modifications enacted by the 82nd Texas Legislature to additional non-grandfathered employees hired before September 1, 2009.	Reduces unfunded liability by an estimated $1.1 billion for high impact/high risk grandfathering.
4.5 Reduces the Amount of Interest Paid on Retirement Account Balances	Reduces the amount of interest paid on employee accounts from 5% per year to a level authorized by the ERS Board of Trustees.	Reduces unfunded liability by an estimated $7.9 million for high impact/high risk grandfathering.
4.6 Establish a 5% per Year Pension Reduction and Eliminate the 25% Cap for Employees Who Retire Prior to Age 60	Establishes a 5% annual pension reduction starting at age 60 for non-grandfathered employees and eliminates the early reduction cap of 25% for those hired after 9/1/09.	Reduces unfunded liability by an estimated $1.1 billion for high impact/high risk grandfathering.
Section 5: Alternative Plan Structures		
5.1 Choice of DC or Modified DB as Mandatory Plan	At the time of employment, this option would provide the member a choice between a DC-only plan and a DB-only plan. The DB option could be the ERS main plan as it is or with plan design modifications.	There would be no unfunded liability for those choosing the DC plan, but an additional contribution of 4.47% would still be needed to make the ERS main plan actuarially sound.
5.2 Cash Balance	Accruals will mimic a DC plan; except the investments are pooled with professional management during active employment and annuitization is required at retirement. The plan will define the benefit in terms of a stated account balance where the investment risks and rewards on plan assets are based on the formula for crediting interest on the notational accounts. Cash balance plans implemented by Nebraska and Louisiana are analyzed.	The actuarial cost, based on two models from other states, range from a low of $7.6 billion to a high of $52.2 billion. By comparison, the agency reports a $8.1 billion to $53.8 billion cost to maintain the current DB plan.
5.3 Two Part Hybrid (DB-DC)	Members participate in a reduced mandatory DB plan and a mandatory DC plan where the combined benefit is intended to provide a benefit while shifting more of the risk to the employee. Employees within certain grandfathered groups remain in the current ERS main DB only plan.	Depends upon the plan design. A sample plan design that maintains the 13% total contribution rate and puts half of the contribution for employees hired after 1/1/2014 into the DC portion of the plan would deplete the trust fund by 2037. Another model with a capped hybrid plan similar to Utah's new plan may be more sound.
5.4 Close DB Plan and Switch to Mandatory DC Plan	New employees are not allowed to participate in the DB plan.	The agency reports the trust fund being depleted by 2039, with an estimated cost to the state that year of $4.3 billion. Of this amount, $3.3 billion is for remaining DB plan members and $925 million is the contribution for the DC plan.

Note[1]: To calculate actuarial impacts, for Options 4.1 to 4.6 the agency ran a high impact/high risk and low impact/low risk variation on each option. The high risk/high impact model grandfathers employees meeting certain criteria as of December 31, 2013, such as being age 50 or older. The low impact/low risk model applies to employees beginning their employment on or after September 1, 2009.
Source: *Retirement Program Report*, Employees Retirement System, September 2012.

Employees Retirement System (ERS)
Group Insurance Program Report

ERS administers the health insurance plan for state employees and retirees. The 2012-13 General Appropriations Act, ERS bill pattern, Rider 13 required the agency to conduct a long-term sustainability study that reviewed plan design and funding. The agency reported seven findings and 37 plan options.

Report Findings:

1. Health insurance benefits are key to attracting and retaining qualified employees.
2. All parties involved with health plan including the Legislature, ERS, and employees/retirees share responsibility for the sustainability of the plan.
3. A sustainable plan would have predictable rate increases.
4. A flexible approach that offers choice and financial incentives will facilitate behavior change.
5. There is a difference between cost management and cost sharing.
6. ERS provides quality benefits at a lower-than-average cost.
7. A long term view is essential since some cost management options may not show immediate savings.

Plan Options and Report Framework:

REPORT SECTION	GOVERNANCE	POLICY QUESTIONS	TYPES OF OPTIONS ANALYZED
Section1 Eligibility	Legislature	Who should be eligible for coverage?	Two options for changing eligibility for certain groups currently covered by the GBP.
Section 2 Contribution Strategy	Legislature	How should the employer and the member share the cost of coverage?	Nine options for changing the contribution strategy for employees, retirees, and/or dependents.
Section 3 Appropriations	Legislature	What is the proper funding level? Does the funding process provide flexibility?	The legislative appropriations process, how the funding process could facilitate sustainability, and how to use appropriated funds to incentivize behavior change.
Section 4 Professional Management	ERS Board of Trustees	How do cost management initiatives save the plan money?	Thirteen options and best practices for managing costs, maximizing the coordination of Medicare benefits contracting, alternative payment systems, and administrative tools.
Section 5 Plan Design	Legislature and Board of Trustees	How can the plan design ensure quality, provide choice, and align incentives with health risks?	Thirteen options for offering plan choice, carving out specialized services, value-based insurance design (VBID), generic drug incentives, and employer solutions.
Section 6 Benchmarking Study	Independent analysis conducted by ERS	How do GBP benefits compare?	Comparison of a “typical” private sector plan against the GBP and reporting on the major features of 13 other large public employer benefit programs (state, county, city, and higher education).

Employees Retirement System
FTE Highlights

Full-Time-Equivalent Positions	Expended 2011	Estimated 2012	Budgeted 2013	Recommended 2014	Recommended 2015
Cap	323.0	332.0	332.0	332.0	332.0
Actual/Budgeted	312.3	313.7	332.0	NA	NA
Schedule of Exempt Positions (Cap)					
Executive Director	$300,000	$312,000	$312,000	$312,000	$312,000

State Auditor's Office Report 12-708, Report on Executive Compensation at State Agencies, indicates a market average of $264,720 for the Executive Director position. Pursuant to Government code, Section 815.208, the Employees Retirement System Board of Trustees has authority to approve the Executive Director's salary. The salary for the Executive Director position was increased from $300,000 to $312,000 in fiscal year 2012.

Pursuant to Government code, section 815.202 (e), the Executive Director prepares an itemized budget annual that the ERS Board of Trustees reviews and adopts. In 2011, the Board of Trustees approved an FTE cap of 332, and it is projected to remain constant for the 2014-15 biennium. ERS is not subject to the Article IX, Section 6.10, Limitation on State Employment Levels, due to the fact that the agency's employees are paid for by funds outside the Treasury, and not by appropriations made in the General Appropriations Act.

Employees Retirement System
Performance Review and Policy Report Highlights

Reports & Recommendations	Report Page	Savings/ (Cost)	Gain/ (Loss)	Fund Type	Included in Introduced Bill	Action Required During Session
Employee Education on Life and Disability Insurance						
1. Include a rider that requires the agency to provide more education on life and disability insurance.	67				Rider 13	

Employees Retirement System
Rider Highlights

1. **(Revise) Informational Listing of Appropriated Funds.** Revise rider to reflect recommendations.

4. **(Revise) State Contribution to Employees Retirement Program.** Revise to reflect a state contribution rate of 6.5 percent for the ERS Retirement fund for each fiscal year of the 2014-15 biennium.

5. **(Revise) State Contribution to Judicial Retirement Program (JRS-2).** Revise rider to reflect a state contribution rate of 6.5 percent for the Judicial Retirement System - Plan 2 for each fiscal year of the 2014-15 biennium.

11. **(Revise) Tobacco User Monthly Premium Fee.** Revise rider to remove contingency provision due to the enactment of legislation and update estimated revenue for the 2014-15 biennium.

12. **(Old) Implement Changes for Medicare Eligible Retirees.** Delete rider due to implementation of Medicare Advantage Program.

12. **(New) State Contribution to the Law Enforcement and Custodial Officer Supplemental Retirement Program (LECOS).** Add new rider to reflect state contribution rate of 0.5 percent for LECOS each year of the 2014-15 biennium.

13. **(Old) Group Insurance Program Study.** Delete rider due to completion of study on September 1, 2012.

13. **(New) Life and Disability Insurance and Education.** Add new rider requiring the agency to provide additional education on life and disability insurance for state employees.

14. **(Old) Contingency for Senate Bill 1811.** Delete rider due to passage of similar legislation related to state contributions of the Law Enforcement and Custodial Officer Supplemental Retirement Fund out of Operators and Chauffeurs License Account No. 99.

Art. IX, Sec. 17.05 (Old Sec. 18.09) **(Revise) Payroll Contribution for Group Health Insurance.** Revise rider to update estimated contributions for the 2014-15 biennium.

Art. IX, Sec. 18.03	**(Old) Pension Plan Changes Study.** Delete rider due to completion of study on September 1, 2012.

Section 6

Employee Retirement System
Items not Included in Recommendations - Senate

	2014-15 Biennial Total	
	GR & GR-Dedicated	All Funds
Agency Exceptional Items - In Agency Priority Order		
1. Provide the consitutional maximum level of funding, 10 percent, to the ERS Retirement fund. This level of funding, with maximum employee contribution of 6.5 percent, is not enough to reach the actuarially sound contribution level of 18.25 percent. The additional needed increase of 1.75 percent would cost another $199,981,250 in All Funds ($129,051,225 in GR and GR-Dedicated).	$ 258,102,449	$ 399,962,500
2. Provide an actuarially sound level of funding to the Law Enforcement and Custodial Officer Supplemental (LECOS) retirement fund, which is an increase of 1.86 percent from the recommended funding level.	$ 50,552,240	$ 55,951,568
3. Provide an actuarially sound level of funding to the Judicial Retirement System - Plan II (JRS-II), which is an increase of 9.02 percent from the recommended funding level. (Total contribution rate of based on an average member contribution of 6.48 percent and a state contribution of 15.52 percent).	$ 7,309,936	$ 12,183,226
4. Funding to provide for 60 days of claims in the Group Benefit Program Reseve Fund, per Insurance Code, Section 1551.211.	$ 187,527,322	$ 297,834,664
Total, Items Not Included in the Recommendations	**$ 503,491,947**	**$ 765,931,958**

	Exp 2011	Est 2012	Bud 2013	Total Biennium 2012-2013	Rec 2014	Rec 2015	Total Rec 2014-2015	Difference
ARTICLE I - GENERAL GOVERNMENT	$30,703,930	$25,542,973	$27,671,555	$53,214,528	$28,241,591	$28,241,591	$56,483,182	$3,268,654
ARTICLE II - HEALTH AND HUMAN SERVICES	$134,543,877	$111,928,689	$121,256,082	$233,184,771	$121,256,082	$121,256,082	$242,512,164	$9,327,393
ARTICLE III - AGENCIES OF EDUCATION	$7,144,543	$5,943,632	$6,438,936	$12,382,568	$6,728,729	$6,728,729	$13,457,458	$1,074,890
ARTICLE IV - THE JUDICIARY	$43,251,037	$34,324,667	$34,867,095	$69,191,762	$34,867,095	$34,867,095	$69,734,190	$542,428
ARTICLE V - PUBLIC SAFETY AND CRIMINAL JUSTICE	$162,016,666	$115,790,167	$133,704,475	$249,494,642	$133,128,118	$133,128,119	$266,256,237	$16,761,595
ARTICLE VI - NATURAL RESOURCES	$28,796,153	$23,955,869	$25,952,193	$49,908,062	$25,952,193	$25,952,193	$51,904,386	$1,996,324
ARTICLE VII - BUSINESS AND ECONOMIC DEVELOPMENT	$54,424,428	$45,276,344	$48,988,751	$94,265,095	$50,211,547	$49,880,392	$100,091,939	$5,826,844
ARTICLE VIII - REGULATORY	$10,217,208	$8,499,819	$9,208,137	$17,707,956	$9,208,137	$9,208,137	$18,416,274	$708,318
ARTICLE X - THE LEGISLATURE	$7,019,515	$5,839,620	$6,326,255	$12,165,875	$6,326,255	$6,326,255	$12,652,510	$486,635
Total	**$478,117,357**	**$377,101,780**	**$414,413,479**	**$791,515,259**	**$415,919,747**	**$415,588,593**	**$831,508,340**	**$39,993,081**
METHOD OF FINANCING:								
General Revenue Funds								
1 General Revenue Fund	$302,462,398	$234,442,620	$263,660,861	$498,103,481	$261,731,608	$262,911,914	$524,643,522	$26,540,041
Subtotal, General Revenue Funds	$302,462,398	$234,442,620	$263,660,861	$498,103,481	$261,731,608	$262,911,914	$524,643,522	$26,540,041
Gr Dedicated								
469 Crime Victims Comp Acct	$0	$0	$0	$0	$0	$0	$0	$0
994 GR Dedicated Accounts	$19,849,911	$16,300,002	$18,099,474	$34,399,476	$17,938,005	$17,956,779	$35,894,784	$1,495,308
Subtotal, Gr Dedicated	$19,849,911	$16,300,002	$18,099,474	$34,399,476	$17,938,005	$17,956,779	$35,894,784	$1,495,308
Federal Funds								
555 Federal Funds	$80,052,232	$66,517,464	$67,169,889	$133,687,353	$68,655,507	$67,125,273	$135,780,780	$2,093,427
Subtotal, Federal Funds	$80,052,232	$66,517,464	$67,169,889	$133,687,353	$68,655,507	$67,125,273	$135,780,780	$2,093,427
Other Funds								
6 State Highway Fund	$69,105,715	$55,627,699	$60,959,727	$116,587,426	$63,043,535	$63,043,535	$126,087,070	$9,499,644
573 Judicial Fund	$0	$0	$0	$0	$0	$0	$0	$0
998 Other Special State Funds	$6,647,101	$4,213,995	$4,523,528	$8,737,523	$4,551,092	$4,551,092	$9,102,184	$364,661
Subtotal, Other Funds	$75,752,816	$59,841,694	$65,483,255	$125,324,949	$67,594,627	$67,594,627	$135,189,254	$9,864,305
Total, Method of Financing	**$478,117,357**	**$377,101,780**	**$414,413,479**	**$791,515,259**	**$415,919,747**	**$415,588,593**	**$831,508,340**	**$39,993,081**

83rd Regular Session, LBB Recommended (Senate), Version 1
Group Insurance

	Exp 2011	Est 2012	Bud 2013	Total Biennium 2012-2013	Rec 2014	Rec 2015	Total Rec 2014-2015	Difference
ARTICLE I - GENERAL GOVERNMENT	$72,146,265	$70,634,685	$76,717,831	$147,352,516	$84,869,161	$92,536,702	$177,405,863	$30,053,347
ARTICLE II - HEALTH AND HUMAN SERVICES	$444,050,199	$434,746,631	$472,715,694	$907,462,325	$516,003,652	$563,401,505	$1,079,405,157	$171,942,832
ARTICLE III - AGENCIES OF EDUCATION	$23,187,454	$22,701,639	$24,734,712	$47,436,351	$27,481,961	$30,060,396	$57,542,357	$10,106,006
ARTICLE IV - THE JUDICIARY	$13,515,934	$13,232,754	$14,437,091	$27,669,845	$15,813,093	$17,325,421	$33,138,514	$5,468,669
ARTICLE V - PUBLIC SAFETY AND CRIMINAL JUSTICE	$413,493,416	$404,830,063	$439,140,658	$843,970,721	$478,194,080	$520,833,186	$999,027,266	$155,056,545
ARTICLE VI - NATURAL RESOURCES	$73,645,577	$72,102,584	$78,501,187	$150,603,771	$85,802,306	$93,808,470	$179,610,776	$29,007,005
ARTICLE VII - BUSINESS AND ECONOMIC DEVELOPMENT	$190,022,260	$186,040,987	$203,574,299	$389,615,286	$226,339,820	$247,914,516	$474,254,336	$84,639,050
ARTICLE VIII - REGULATORY	$24,726,917	$24,208,848	$26,316,632	$50,525,480	$28,719,287	$31,349,296	$60,068,583	$9,543,103
ARTICLE X - THE LEGISLATURE	$17,788,894	$17,416,188	$18,966,751	$36,382,939	$20,736,318	$22,677,341	$43,413,659	$7,030,720
Total	**$1,272,576,916**	**$1,245,914,379**	**$1,355,104,855**	**$2,601,019,234**	**$1,483,959,678**	**$1,619,906,833**	**$3,103,866,511**	**$502,847,277**
METHOD OF FINANCING:								
General Revenue Funds								
1 General Revenue Fund	$781,932,777	$765,550,026	$834,110,273	$1,599,660,299	$916,952,397	$1,003,217,717	$1,920,170,114	$320,509,815
Subtotal, General Revenue Funds	$781,932,777	$765,550,026	$834,110,273	$1,599,660,299	$916,952,397	$1,003,217,717	$1,920,170,114	$320,509,815
Gr Dedicated								
994 GR Dedicated Accounts	$45,478,591	$44,525,741	$48,769,164	$93,294,905	$53,473,906	$58,584,016	$112,057,922	$18,763,017
Subtotal, Gr Dedicated	$45,478,591	$44,525,741	$48,769,164	$93,294,905	$53,473,906	$58,584,016	$112,057,922	$18,763,017
Federal Funds								
555 Federal Funds	$246,542,042	$241,376,588	$259,937,832	$501,314,420	$276,082,933	$297,897,046	$573,979,979	$72,665,559
Subtotal, Federal Funds	$246,542,042	$241,376,588	$259,937,832	$501,314,420	$276,082,933	$297,897,046	$573,979,979	$72,665,559
Other Funds								
6 State Highway Fund	$193,665,153	$189,607,557	$207,007,523	$396,615,080	$231,659,386	$253,883,534	$485,542,920	$88,927,840
998 Other Special State Funds	$4,958,353	$4,854,467	$5,280,063	$10,134,530	$5,791,056	$6,324,520	$12,115,576	$1,981,046
Subtotal, Other Funds	$198,623,506	$194,462,024	$212,287,586	$406,749,610	$237,450,442	$260,208,054	$497,658,496	$90,908,886
Total, Method of Financing	**$1,272,576,916**	**$1,245,914,379**	**$1,355,104,855**	**$2,601,019,234**	**$1,483,959,678**	**$1,619,906,833**	**$3,103,866,511**	**$502,847,277**