Primer on Benefits for State Employees and Public and Higher Education Employees

PREPARED BY LEGISLATIVE BUDGET BOARD STAFF

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PRIMER ON BENEFITS FOR STATE EMPLOYEES AND PUBLIC AND HIGHER EDUCATION EMPLOYEES

INTRODUCTION

This primer will serve as a guide for the Legislature on state of Texas retirement and health insurance benefit systems. The primer focuses on retirement eligibility, funding structure and history of the Employees Retirement System, Teacher Retirement System, and Optional Retirement Program. The primer also includes basic insurance components of the Employees Retirement System, Higher Education Group Insurance, and the Teacher Retirement System (active and retiree members), including insurance funding and benefit structure and premiums.

RETIREMENT

EMPLOYEES RETIREMENT SYSTEM

HISTORY

In 1945, the Forty-ninth Legislature of the State of Texas passed House Joint Resolution 10, a constitutional amendment that allowed Texans to vote to approve or reject the constitutional formation of a Retirement, Disability, and Death Compensation Fund for state employees. It was approved, and on June 10, 1947, Governor Beauford Jester signed the bill, establishing the Employees Retirement System (ERS) and implementing the constitutional amendment effective September 1, 1947. ERS's responsibilities have expanded since then as a result of legislative action over the years. Legislation passed in 1954 by the Fifty-fourth Legislature transferred the administration of the Judicial Retirement System of Texas to ERS. In 1963, a new law expanded ERS membership to include elected state officials, including legislators. District attorneys were included by the Sixtieth Legislature in 1967. In 1979, the Law Enforcement and Custodial Officer Supplemental (LECOS) Retirement Fund was established to provide an increased retirement benefit for Certified Peace Officers and Custodial Officers. In 1985, the creation of a Judicial Retirement System Plan II was authorized to phase out the Judicial Retirement System Plan I that the ERS had administered since 1954. On January 1, 2008, Texas began auto enrollment of all new hires of state agencies into the TexaSaver 401K Plan. These new hires can choose not to participate within their first 30 days of employment.

In 1950, Congress created Section 218 of the Social Security Act. Effective January 1, 1951, federal law allowed states to enter into voluntary agreements with the Social Security Administration (SSA) for social security coverage for their state and local governments. The State of Texas entered into a federal-state agreement with the Social Security Administration effective January 1, 1951. The Texas Legislature delegated the responsibility for the administration of the Texas Social Security Program for state and local governments with the Department of Public Welfare beginning in 1951. Administrative responsibilities were then transferred to the Employees Retirement System of Texas in 1975. As the administrator, ERS has oversight for administering referendums, or elections, held by political subdivisions which provide for Social Security or Medicare Only coverage for employees of state and local governments.

Before fiscal year 1996, state employees received a state paid Federal Insurance Contributions Act (FICA) supplemental payment of 5.85 percent on their first $16,500 of FICA-covered wages, up to a maximum of $965.25. The Seventy-fourth Legislature, Regular Session, 1995, repealed this additional state-paid contribution for the social security obligation for employees on the payroll as of August 31, 1995, and replaced it with a benefit supplement to ensure that take-home pay was not reduced.

GOVERNANCE AND POLICY

ERS is governed by a board of six trustees who serve staggered six-year terms. By statute, three are active state employees who are elected by the members of the system. The remaining three are appointed, one each by the Governor, the Speaker, and the Chief Justice of the Texas Supreme Court. As fiduciaries of ERS's funds, ERS's Board of Trustees investment policies are governed by the Texas Trust Code and the Texas State Constitution.

The Board's mission is to:

- Earn a return that will insure the payments due to members of the retirement plans and their beneficiaries;
- Manage fund assets for the exclusive benefit of the members of the retirement plans;
- Assist the trustees to develop prudent investment policies defining investment objectives and strategies;

- Seek to maximize investment return while maintaining acceptable levels of risk;
- Reduce risk through diversification; and
- Efficiently manage the costs associated with implementation of the investment program.

A staff of trained professional personnel, in accordance with trustee policies and constitutional and statutory regulations, invests state contributions, member contributions, and investment income. To assist the staff with investment recommendations and decisions, the Trustees have employed investment managers and have appointed an Investment Advisory Committee composed of members of the financial and business community of Texas. Also, ERS retains an independent consultant to evaluate and analyze investment results.

MEMBERSHIP

Figure 1 shows the membership numbers for ERS, the Law Enforcement and Custodial Officer Supplemental (LECOS) Retirement Fund, the Judicial Retirement System of Texas Plan One (JRS-I), and the Judicial Retirement System of Texas Plan Two (JRS-II) as of August 31, 2007. Non-contributing members refers to those former employees who have not withdrawn their retirement funds.

FIGURE 1
MEMBERSHIP AS OF AUGUST 31, 2008

	ACTIVE MEMBERS	NON-CONTRIBUTING MEMBERS	RETIREES AND BENEFICIARIES
ERS	134,626	74,094	72,678
LECOS*	33,642	35	6,204
JRS-I	27	7	471
JRS-II	518	120	117

*Members of LECOS are also members of ERS.
Source: Employees Retirement System.

There are two distinct classes of membership within the ERS. The first class is the Employee Class, which includes employees and appointed officers of every department, commission, board, agency, or institution of the state except those included in the coverage of the Teacher Retirement System (TRS), those participating in the Optional Retirement Program (ORP), and those in the two retirement plans for judges: JRS I and JRS II. The second class is the Elected Class, which includes those who hold state offices that are normally filled by statewide election and that are not included in the coverage of JRS I and JRS II. This includes members of the Legislature, as well as district and criminal district attorneys. **Figure 2** shows ERS membership from 1998 to 2008.

Members of the LECOS Retirement Fund are also members of ERS. This plan covers law enforcement officers commissioned by the Department of Public Safety, the Alcoholic Beverage Commission, and the Parks and Wildlife Department recognized as commissioned law enforcement officers by the Commission on Law Enforcement Officer Standards and Education. The plan also covers custodial officers employed by the Department of Criminal Justice, including the Board of Pardons and Paroles, and certified by that department according to statutory requirements as having a normal job assignment that requires frequent or infrequent planned contact with inmates of that institution.

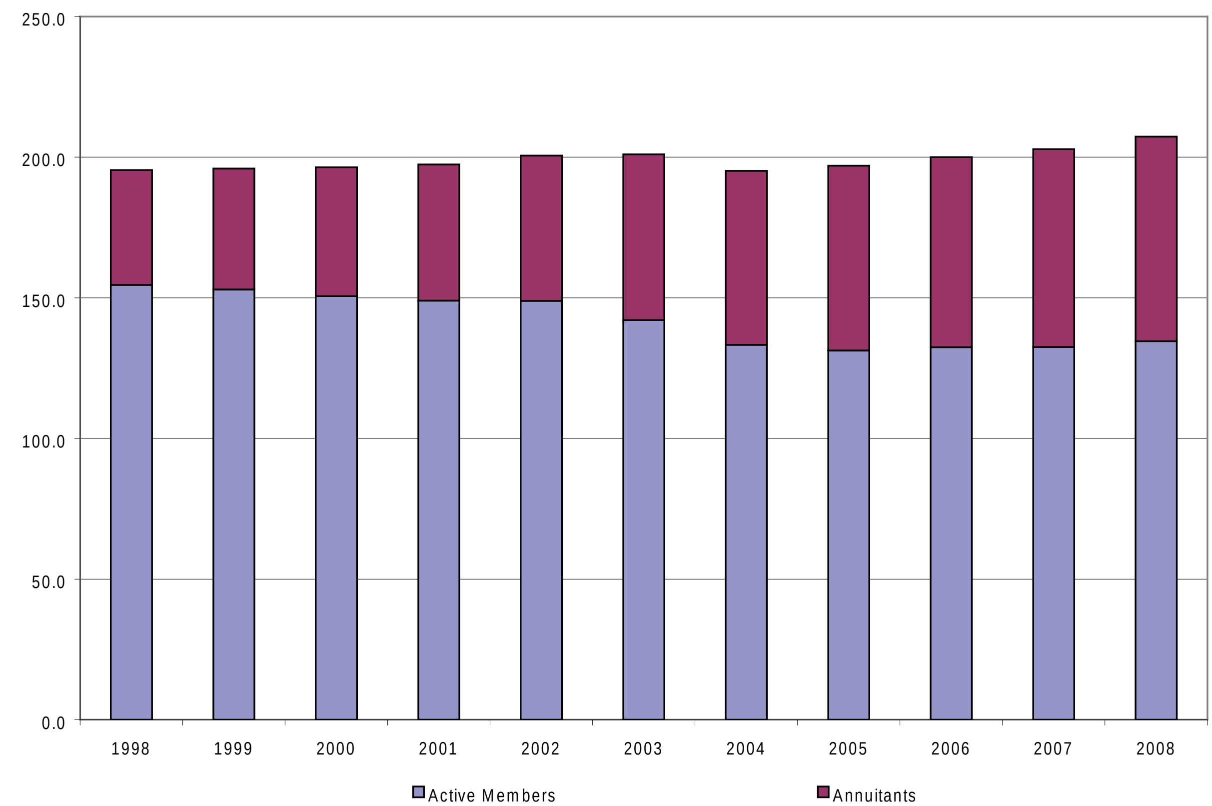
JRS I is for judges, justices and commissioners of the Supreme Court, the court of Criminal Appeals, the Court of Appeals, District Courts, and certain commissions to a court whose service began before September 1, 1985. Those whose service began on or after September 1, 1985 are members of JRS II.

CONTRIBUTIONS

The programs administered by ERS are funded by a combination of state appropriations for state contributions, member contributions, and investment earnings. The administrative costs to operate these programs are not appropriated, but instead are funded from monies available, including investment earnings, within each of the respective funds.

Under the Texas Constitution, the state's contribution for employees' retirement may not exceed 10 percent of total payroll except in an emergency declared by the Governor, nor may it be less than 6 percent. The percentage of payroll that the state currently contributes is specified via rider under the ERS appropriation in the General Appropriations Act. Currently, these state contribution rates are 6.45 percent for ERS Retirement, 1.59 percent for LECOS, and 16.83 percent for JRS II. Using the appropriate percentage, each agency sends the appropriate state contribution along with the member contribution (currently 8 percent of gross salary for legislators and 6 percent of gross salary for all others) to ERS as each payroll is processed during the year. ERS has an actuarial valuation report prepared each year and mid-year for each of these plans during a legislative session. An actuarial valuation is a report on the position of the pension plan at a

FIGURE 2
EMPLOYEES RETIREMENT SYSTEM MEMBERSHIP
(IN THOUSANDS)



Source: Employees Retirement System.

given point in time. The valuation includes a measurement of the plan's accrued liability and compares it to the plan's assets, then analyzes the reasons for changes from the previous year. The valuation also determines the actuarial soundness of the total contribution rate to the pension plan, meaning the contributions must be sufficient to fund the normal cost plus amortize the unfunded accrued liability over no more than 31 years. These valuations form the basis of the ERS requests for funding during the legislative session. Rather than being prefunded on an actuarial basis, JRS I is funded on a pay-as-you-go basis, meaning the funds required for monthly annuity payments and refunds of member contributions are appropriated for each fiscal year out of the General Revenue Fund.

ERS, LECOS, and JRS II funding are "estimated" appropriations at the end of each article of the General Appropriations Act (GAA). This type of appropriation means that ERS has the authority to increase the appropriation as needed within the parameters of the GAA. The total appropriation for all articles is shown as an informational listing in the ERS appropriation pattern. **Figure 3** summarizes the appropriation history for the retirement programs as well as health insurance.

INVESTMENT POLICY

In the beginning, ERS was limited to investing only in government securities. During its first year, the $2.9 million in member and state contributions was invested in U. S. bonds. In 1958, investments were allowed, within specific parameters, in corporate securities, common stocks, preferred stocks, debentures, bonds, mortgages, etc. The first investment in corporate stocks was in 1960 when ERS purchased 10,000 shares in 30 corporations at a cost of $614 million.

ACTUARIAL VALUATION

The February 28, 2009 actuarial valuation update (the latest actuarial valuation as of this writing) shows that the ratio of the actuarial value of assets to the actuarial accrued liability was 88.9 percent, which is a decrease of 3.7 percentage

FIGURE 3
APPROPRIATION HISTORY (IN MILLIONS)
(2005–2009)

	2005	2006	PERCENTAGE CHANGE	2007	PERCENTAGE CHANGE	2008	PERCENTAGE CHANGE	2009	PERCENTAGE CHANGE
RETIREMENT									
ERS	$275.0	$313.9	14.1	$327.7	4.4	$339.1	3.5	$354.2	4.4
LECOS	--	--	N/A	--	N/A	20.3	N/A	20.5	1.0
JRS-I	22.4	27.8	24.0	29.0	4.4	28.8	(0.9)	29.1	1.0
JRS-II	8.4	10.1	20.3	11.0	8.8	11.1	1.8	11.3	1.0
RETIREMENT SUBTOTAL	**$305.8**	**$351.8**	**15.0**	**$367.7**	**4.5**	**$399.3**	**8.6**	**$414.9**	**3.9**
HEALTH INSURANCE									
ERS	$879.6	$967.1	9.9	$1,022.0	5.7	$1,041.3	1.9	$1,078.3	3.6
HEGI	205.7	243.6	18.4	257.4	5.7	272.2	5.7	118.2	(56.6)*
UT	124.7	139.3	11.7	147.2	5.7	152.3	3.5	152.3	0.0
A&M	67.6	73.1	8.1	77.3	5.7	79.0	2.2	79.0	0.0
INSURANCE SUBTOTAL	**$1,277.7**	**$1,423.1**	**11.4**	**$1,503.8**	**5.7**	**$1,544.8**	**2.7**	**$1,427.8**	**(7.6)**
TOTAL	**$1,583.5**	**$1,774.9**	**12.1**	**$1,871.5**	**5.4**	**$1,944.1**	**3.9**	**$1,842.7**	**(5.2)**

*The Governor vetoed the 2009 funding for HEGI contributions for Public Community/Junior Colleges.
Source: Legislative Budget Board.

points from the August 31, 2008 valuation. Because the total contribution rate of 12.45 percent of payroll is not sufficient to amortize the unfunded accrued liability, the current amortization period is infinite and the funding objective is not being met. According to the most recent valuation, for fiscal year 2009, the total required contribution rate that would both fund the normal cost and amortize the unfunded accrued liability over 31 years as a level percentage of payroll is 19.38 percent. This is an increase of 3.93 percentage points from the August 31, 2008 valuation. Texas Government Code precludes any supplemental payments, such as a 13th check to retirees, or increase in annuity benefits unless the total contribution is at a rate to fund the normal cost and amortize the unfunded accrued liability over less than 31 years. According to the February 28, 2009 actuarial valuation update, the market value of the ERS retirement fund is approximately $15.0 billion, a decrease of $6.4 billion from the August 31, 2008 valuation. (During the third quarter of 2008, the United States equity markets began to suffer significant losses due to the devaluing of mortgage-backed securities and the resulting tightening of credit issued by lenders. This downturn in the economy resulted in the decrease of the market value of the ERS Pension Trust Fund.) **Figure 4** shows a ten-year history of the ERS Pension Trust Fund's investment returns compared to its actuarially assumed rate of return.

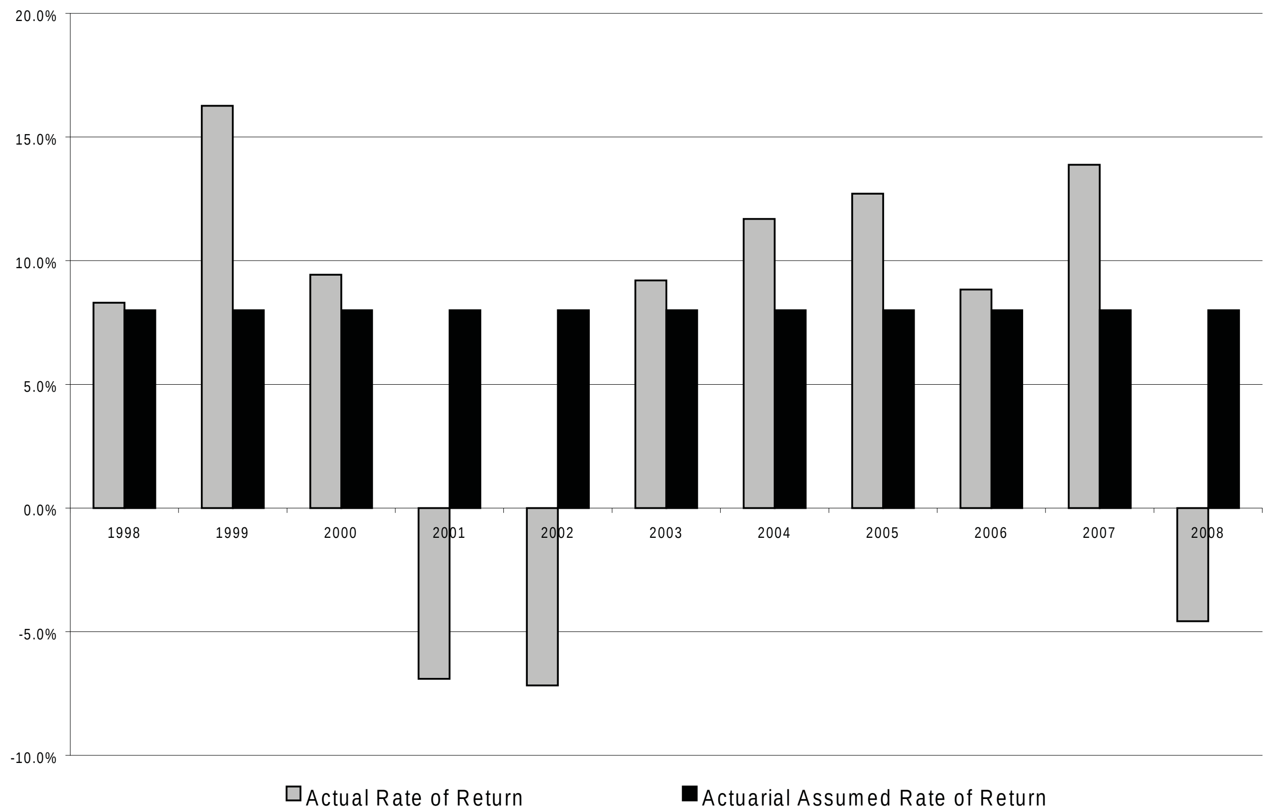
ELIGIBILITY REQUIREMENTS

Figure 5 summarizes the eligibility requirements for members of the ERS retirement plans to receive benefits. This is referred to as "becoming vested." To become vested means to be securely qualified to receive a lifetime retirement annuity.

Service credit refers to the length of time worked and may also include purchased active duty military time, months of unused sick and annual leave, and other eligible service. The purchase of additional service credit is available through ERS to allow individuals to retire earlier or increase the amount of their annuity payment.

The LECOS retirement plan and the two judicial plans, JRS I and JRS II, have provisions that allow early service retirement with reduced benefits. This means members are eligible to retire before they meet the eligibility requirements in **Figure 5**, but their benefits are reduced compared to the standard retirement annuity. The amount of the reduction is calculated based on the member's age at the time of retirement. Eligibility requirements for early service retirement with reduced benefits are listed in **Figure 6**.

FIGURE 4
ERS RETIREMENT TRUST FUND ACTUAL ANNUAL RETURN ON INVESTMENTS COMPARED TO ASSUMED ANNUAL RETURNS
1998–2008



SOURCE: Employees Returment System.

FIGURE 5
SERVICE RETIREMENT ELIGIBILITY

ERS	LECOS	JRS I AND JRS II
Employee Class Only: • Age 60 with at least 5 years of service credit, or • The sum of age and years of service credit equals or exceeds the number 80 (“Rule of 80”) with at least 5 years of service credit, or • Age 55 with at least 10 years of service credit as a certified peace officer or custodial officer. **Elected Class Only:** • Age 60 with 8 years of service credit, or • Age 50 with 12 years of service credit.	• 20 years of service credit as a certified peace officer/custodial officer and the member’s age is the earlier of either the age of 50 or the age at which the sum of age and years of service credit equals or exceeds the number 80 (“Rule of 80”).	• Age 65 with at least 10 years of service credit and currently holding a judicial office, or • Age 65 with at least 12 years of service credit, regardless of whether the member currently holds a judicial office, or • 20 years of service at any age, regardless of whether the member currently holds a judicial office, or • The sum of age and years of service equals or exceeds the number 70 (“Rule of 70”) and served at least 12 years on an appellate court, regardless of whether the member currently holds a judicial office.

SOURCE: Employees Retirement System.

FIGURE 6
EARLY SERVICE RETIREMENT WITH REDUCED BENEFITS

ERS	LECOS	JRS I AND JRS II
Not applicable.	• 20 years of service credit as a certified peace officer/custodial officer, under the age of 50.	• Age 60 with 10 years of service credit and currently holding a judicial office, or • Age 60 with 12 years of service credit, regardless of whether the member currently holds a judicial office.

Source: Employees Retirement System.

BENEFITS

For those members who meet the standard retirement eligibility requirements, **Figure 7** summarizes the plans' provisions with regard to the standard retirement benefits.

All of the retirement programs administered by ERS have optional benefits that members can choose with regard to their beneficiaries. By choosing none of the survivor benefits, the member will receive the standard retirement annuity using the calculation methods in **Figure 5**. However, if the member chooses one of the available survivor benefit options, his or her monthly annuity is reduced, depending on the option chosen. Should the beneficiary predecease the retired member, the annuity paid to the member is increased to the standard annuity. The retirement programs' optional benefits provisions are summarized in **Figure 8**.

Figure 9 shows annual ERS service retirements since 1998.

DISABILITY BENEFITS

There are two types of disability retirement benefits available to members of ERS: occupational and non-occupational. An occupational disability is defined by ERS as "a sudden and unexpected injury or disease that results solely from a specific act or occurrence determinable by a definite time and place and solely from an extremely dangerous risk of severe physical or mental trauma or disease that is not common to the public at large and that is peculiar to and inherent in a dangerous duty that arises from the nature and in the course of a person's state employment." A non-occupational disability does not have to be related to the work being performed. A qualifying example of a non-occupational disability retirement is when an employee is diagnosed with a terminal illness and is unable to continue working.

Eligibility requirements for both types of disability are summarized in **Figure 10**.

FIGURE 7
STANDARD SERVICE RETIREMENT BENEFITS

ERS	LECOS	JRS I AND JRS II
Employee Class Only: • Monthly annuity is equal to 2.3% of average monthly compensation multiplied by the number of years of service credit. • Average monthly compensation is the average of the highest 36 months of compensation. • Minimum standard annuity is $150 per month. • Maximum standard annuity is 100% of the average monthly compensation. **Elected Class Only:** • Monthly annuity is 2.3% of the current salary of a district judge multiplied by the number of years of service credit. • Retirement benefits are automatically adjusted as State judicial salaries increase. • Maximum standard annuity is 100% of the salary being paid a district judge.	• Monthly annuity is equal to 2.8% of average monthly compensation multiplied by the number of years of service credit. • Average monthly compensation is the average of the highest 36 months of compensation. • Minimum standard annuity is $150 per month. • Maximum standard annuity is 100% of the average monthly compensation.	• Monthly annuity is equal to 50% of the salary for the position from which the member retired. • An additional 10% is paid when a member retires within one year of leaving office or within one year of last assignment as a visiting judge. • The monthly annuity of a member who elects to make contributions after 20 years of service would be based on 50% of salary plus 2% for each subsequent year with the total, including the additional 10%, not to exceed 90%. **JRS II only:** • The monthly annuity of a member who elects to make contributions after reaching the Rule of 70 with at least 12 years on an appellate court would be based on 50% of the State salary plus 2.3% for each subsequent year with the total, including the additional 10%, not to exceed 90%.

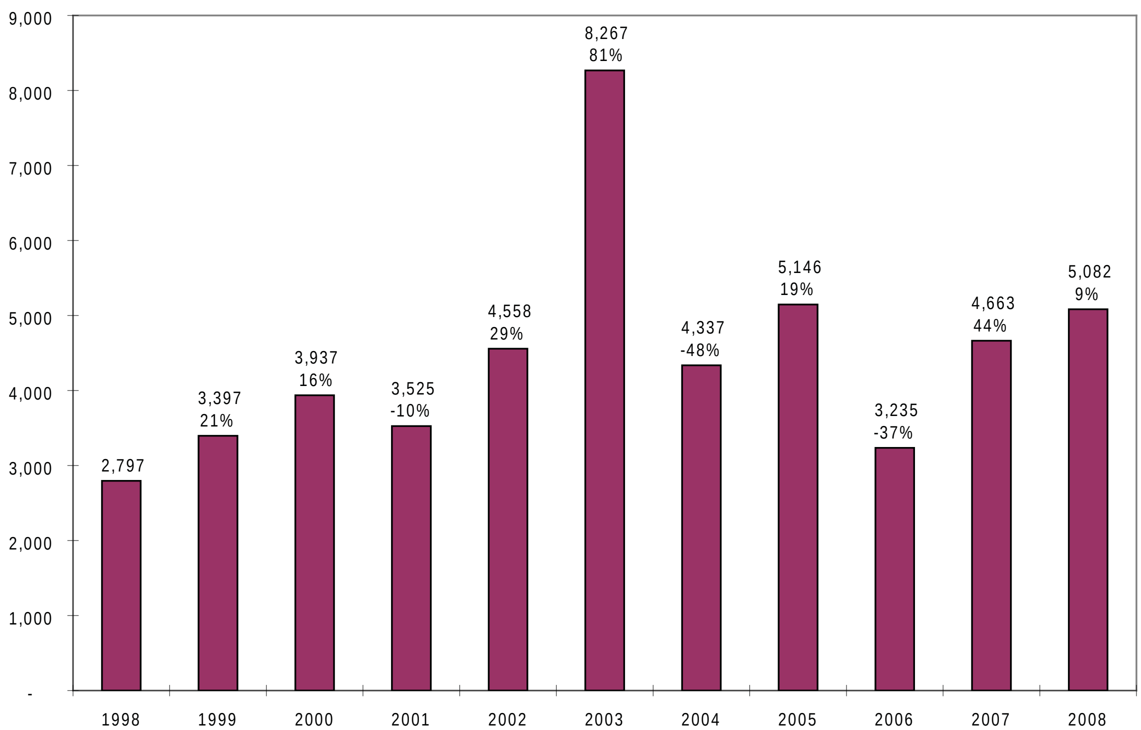
Source: Employees Retirement System.

FIGURE 8
OPTIONAL SERVICE RETIREMENT BENEFITS

ERS	LECOS	JRS I AND JRS II
Employee Class and Elected Class:		
• Lifetime annuity for member with 100% of the annuity to surviving beneficiary for life; • Lifetime annuity for member with 75% of the annuity to surviving beneficiary for life; • Lifetime annuity for member with 50% of the annuity to surviving beneficiary for life; • Lifetime annuity for member. If member dies before receiving five years (60 months) of annuity payments, the beneficiary receives the remainder of those 60 payments. • Lifetime annuity for member. If member dies before receiving ten years (120 months) of annuity payments, the beneficiary receives the remainder of those 120 payments. • One-time partial lump sum of up to 3 years of standard annuity at retirement (annuity is reduced for life and the reduced annuity is used to calculate above beneficiary options.)	• Same as Employee Class.	• Same as Employee Class except for the one-time partial lump sum provision.

SOURCE: Employees Retirement System.

FIGURE 9
ANNUAL SERVICE RETIREMENTS AND ANNUAL PERCENT CHANGE
1998–2008



SOURCE: Employees Retirement System.

FIGURE 10
DISABILITY RETIREMENT ELIGIBILITY

ERS	LECOS	JRS I AND JRS II
Employee Class Only: • For occupational disability, no age or length of service requirement. • For non-occupational disability, at least 10 years of service credit, which may include up to 5 years of purchased military service credit, and be a contributing member. **Elected Class Only:** • For occupational disability, no age or length of service requirement. • For non-occupational disability, eight years of service (exclusive of military service) or 6 years service plus 2 years of military service if purchased before 1/1/78, and be a contributing member.	• Same as Employee Class.	• No age requirement. • Seven years of judicial service and currently holding a judicial office.

Source: Employees Retirement System.

Members must meet the conditions for one of the types of disability above in order to receive the retirement annuity and insurance benefits. **Figure 11** summarizes disability retirement benefits for each of the retirement programs.

PROPORTIONATE RETIREMENT

The Employee Retirement System and the Judicial Retirement System of Texas currently participate in the proportionate retirement program. This program allows a member with

FIGURE 11
DISABILITY RETIREMENT BENEFITS

ERS	LECOS	JRS I AND JRS II
Employee Class Only: • For occupational disability, the benefits are the same as those under the standard service retirement, except the standard annuity is equal to not less than 35% of the average of the highest 36 months of compensation regardless of the years of service credit or age. • For non-occupational disability, the retirement benefits are actuarially reduced from normal retirement eligibility based on age and length of service. • The optional annuity plans available are the same as those under a service retirement except for the partial lump-sum option. There is no early service retirement eligibility with reduced benefits. **Elected Class Only:** • For both occupational and non-occupational disability, the standard annuity is 18.4% of the State salary of a district judge, or 2.3% of the State salary of a district judge times years of Elected Class service, whichever is greater. • Optional annuity plans available are the same as those under a service retirement except for the partial lump-sum option.	• For occupational disability, the standard annuity is a minimum of 50% of the average of the highest 36 months of compensation regardless of the years of service credit or age. • The standard annuity is increased to 100% of the average of the highest 36 months of compensation if a member receives Social Security disability benefits as a result of occupational disability. • For non-occupational disability, the retirement benefits are actuarially reduced from normal retirement eligibility based on age and length of service. • The optional annuity plans available are the same as those under a service retirement except for the partial lump-sum option.	• Same as standard service retirement benefits without reduction for age.

Source: Employees Retirement System.

active membership credit in more than one Texas public statewide retirement system to combine all of his or her service credit to satisfy eligibility requirements.

DEATH BENEFITS FOR RETIREEES

Upon the death of an ERS retiree, a lump sum of $5,000 is paid to his or her beneficiary(ies). This state paid benefit is for retireers receiving an annuity from ERS, even if they do not qualify for insurance in retirement. A member who retires proportionately and has less than five years of ERS service credit can receive a reduced lump sum death benefit.

TEACHER RETIREMENT SYSTEM

HISTORY

In 1936, voters approved an amendment to the State Constitution creating a statewide teacher retirement system to serve the needs of public education employees. The Texas Legislature passed enabling legislation in 1937 to form the Teacher Retirement System of Texas (TRS), a pension fund, to provide benefits for persons employed in the public schools, colleges, and universities. The system currently operates under Section 67, Article XVI of the Texas Constitution.

GOVERNANCE AND POLICY

TRS is governed by a nine-member board of trustees who serve staggered six-year terms. Three trustees are direct appointments by the Governor and are persons who have demonstrated financial expertise, have broad investment experience, and are not active or retired members of the system. Two trustees are appointed by the Governor from a list of candidates offered by the State Board of Education. The remaining five trustee appointments are selected from a list of the three top vote-getters in an election among active and retired employees of public schools and higher education. The board is responsible for the prudent management of assets held in the trust, seeking long-term investment returns that exceed the established actuarial rate of return.

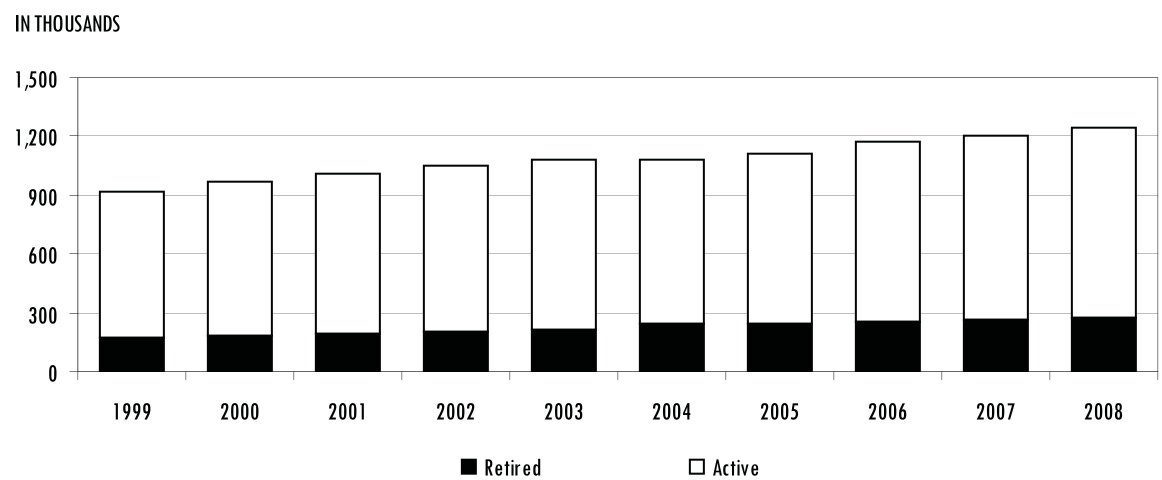
MEMBERSHIP

Membership in TRS is a condition of employment for all employees of public, state-supported educational institutions who work at least 20 hours or more per week and at least 4 ½ months or more in one school year. Employees who are employed in membership-eligible positions are required to participate in TRS and are automatically enrolled in TRS on their first day of employment. Unless excluded from membership by law, participation in TRS cannot be waived. As of August 31, 2008, there were 966,043 active members in the system, an increase of 30,312 members above fiscal year 2007. **Figure 12** shows the growth of TRS membership, both active and retired, since fiscal year 1999.

CONTRIBUTIONS

The TRS retirement system is funded by member, state, and employer contributions to the trust fund and through investment earnings on the trust fund. Contribution rates are established by law and are intended to remain level as a percentage of payroll. The contributions for fiscal year 2008 are summarized in **Figure 13**.

FIGURE 12
TEACHER RETIREMENT SYSTEM MEMBERSHIP, FISCAL YEARS 1999 TO 2008



Source: Teacher Retirement System.

FIGURE 13
TRS RETIREMENT TRUST FUND ACTUAL 2008 CONTRIBUTIONS

	STATE CONTRIBUTION	LOCAL DISTRICTS	STATUTORY MINIMUM	GENERAL REVENUE– DEDICATED	NEW MEMBER FIRST 90 DAYS	TOTAL CONTRIBUTIONS
Public Education	$1,303,366,372	$125,730,278	$211,412,173	NA	$33,187,903	$1,673,696,727
Higher Education	$160,003,071*	$109,271,768	NA	$84,365,558	$13,576,562	$367,217,858

*Higher Education state contributions include funding from the Pension Trust Fund for TRS employee retirement.
Source: Teacher Retirement System.

The State Constitution provides for a state contribution rate in the range of 6 percent to 10 percent per year. **Figure 14** summarizes the components of contributions for public education and higher education for fiscal year 2008.

The Eightieth Legislature, 2007, enacted several laws affecting TRS active members, retirees, and investments. Senate Bill 1846 established a provision in statute that stipulates the state contribution rate may not be less than the contribution rate of active members and authorized the TRS Board of Trustees to provide a one-time benefit increase to annuitants equal to their monthly annuity paid in August 2007, not to exceed a cap of $2,400. The 2008–09 active member contribution rate is set at 6.4 percent and the state contribution rate is 6.58 percent. The state rate for new members during the first 90 days of employment is paid by the employer. **Figure 15** summarizes the appropriation history for the TRS retirement programs as well as TRS-Care retiree health insurance.

INVESTMENTS

The TRS Board oversees the investment of the pension system's funds in order to achieve long-term investment returns. In 2007, a comprehensive review of TRS investment policies and practices was conducted and initiatives were developed to help the fund meet its future obligations. The initiatives centered on providing a more efficient asset allocation, accessing external managers where appropriate, using derivative instruments to manage risks in a proactive manner and establishing risk management principles and

FIGURE 14
TRS RETIREMENT FUNDING SOURCES

PUBLIC EDUCATION AND HIGHER EDUCATION	
CONTRIBUTOR	**CONTRIBUTION BASIS**
State	6.58%
Employee	6.40%
Employer – Public Education	Statutory Minimum, First 90 Days, Federal Funds and Private Grants
Employer – Higher Education	Other Education & General Income (not paid from GR), First 90 Days, Federal Funds and Private Grants
Retirement Trust Fund	Investment Income

Source: Teacher Retirement System.

FIGURE 15
APPROPRIATION HISTORY (IN MILLIONS)
2006–2009

	2006	PERCENTAGE CHANGE	2007	PERCENTAGE CHANGE	2008	PERCENTAGE CHANGE	2009	PERCENTAGE CHANGE
RETIREMENT								
Public Education	$1,114.2	3.8	$1,243.2	11.6	$1,303.4	4.8	$1,357.7	4.2
Higher Education	$282.1	8.8	$298.6	5.9	$244.3	(18.2)	$253.9	3.9
Retirement Subtotal	**$1,396.3**	**4.7**	**$1,541.8**	**10.4**	**$1,547.7**	**0.4**	**$1,611.6**	**4.1**
HEALTH INSURANCE								
TRS-Care	$214.0	4.8	$237.6	11.0	$232.6	(2.1)	$243.2	4.5
TOTAL	**$1,610.3**	**4.8**	**$1,779.4**	**10.5**	**$1,780.3**	**.05**	**$1,854.8**	**4.2**

Source: Teacher Retirement System.

practices. In previous years, fund returns were driven primarily by investments in large cap domestic equities. New investment legislation established under Senate Bill 1447, Eightieth Legislature, 2007, broadened the investment authority on investment products such as futures contracts, options, swaps, and other investment tools. The legislation also allows the board to delegate to external investment managers up to 30 percent of the portfolio and limits investments in hedge funds to 5 percent of the portfolio. The investment authority expires in five years unless re-authorized by the legislature. TRS has expanded the role of alternative investments in its overall investment strategy, which emphasizes effective diversification, risk management, talent attraction, and long-term performance. Other legislation passed by the Eightieth Legislature, 2007, established a divestment procedure for investments by TRS in certain entities doing business in Sudan.

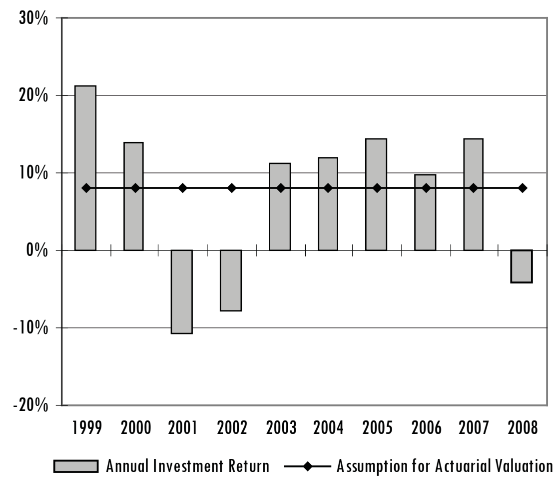
ACTUARIAL VALUATION

An actuarial valuation is conducted annually, as of August 31 of each year, the last day of the System's plan and fiscal year. Valuations determine the adequacy of the current state contribution rate by measuring the current solvency of the value of the pension fund's assets against its liabilities. The TRS retirement trust fund is considered actuarially sound if its funding is sufficient to cover its "normal cost" (the percentage of payroll needed to fund plan benefits for new members) and to pay off any unfunded liabilities over a period of less than 31 years. The unfunded liability is the portion of the actuarial cost of future benefits that exceeds the actuarial value of current assets.

A revised, but limited, actuarial valuation as of February 28 is conducted during the years when the Legislature meets in regular session. The February 28, 2009 actuarial valuation update reveals that the market value of the TRS retirement fund decreased in value to $70.6 billion, or 32 percent, from the previous actuarial report on August 31, 2008. The total required state contribution rate to meet the 30-year statutory benchmark is 11.25 percent of pay if the members' rate remains at 6.40 percent of pay. The funded ratio of the plan's assets over the plan's liabilities has decreased to 67.7 percent, down 22.8 percentage points from the August 31, 2008 actuarial valuation.

The Eightieth Legislature, 2007, authorized the TRS Board to make a one-time payment (13th check) to annuitants, provided the Retirement Trust Fund was actuarially sound based on the August 31, 2007 actuarial valuation. TRS made the 13th check payment in January 2008 to annuitants equal to the amount of the monthly annuity payment to which an eligible annuitant was entitled in August 2007, not to exceed $2,400. **Figure 16** shows the annual rate of return on investment for the retirement trust fund's assets since fiscal year 1999.

FIGURE 16
TRS RETIREMENT TRUST FUND ACTUAL ANNUAL RETURN ON INVESTMENT COMPARED TO ASSUMED ANNUAL RETURN, FISCAL YEARS 1999 TO 2008



SOURCE: Teacher Retirement System.

ELIGIBILITY

Normal-age service retirement eligibility includes:

a. A member who became a member of TRS prior to September 1, 2007 and maintained membership until retirement becomes eligible when the member (1) attains age 65 with at least 5 years of service credit, or (2) attains a combined number of years of age and service credit that totals 80.

b. A member who became a member of TRS or returned to membership on or after September 1, 2007 becomes eligible when the member (1) attains age 65 with at least 5 years of service credit, or (2) has attained age 60 with at least 5 years of service credit and has a combined number of years of age and service credit that totals 80.

c. Grandfathered members who terminate their TRS membership by withdrawal of contributions at any time (prior to or after September 1, 2007) and return to membership on or after September 1, 2007 become eligible for unreduced benefits when the member (1) attains age 65 with at least 5 years of service credit, or (2) attains age 55 with at least 5 years of service credit and meets the Rule of 80 (combined number of years of age and service credit that totals 80).

Grandfathered members who return to membership on or after September 1, 2007 are subject to a 5 percent reduction for each year under age 60 if they retire before age 55 and meet the Rule of 80. Members with at least 30 years of service credit but who do not meet the Rule of 80 also have a 5 percent reduction for each year under age 60.

Normal-age service retirement annuity calculations are based on the standard annuity, which provides the retiree a maximum amount of benefit each month (compared to optional service retirements) and ends upon the retiree's death. A standard annuity is a monthly benefit payable at retirement throughout the retiree's lifetime.

The annual standard annuity equals 2.3 percent times the average of the five highest annual creditable salaries times years of credited service.

Members have five options for annuity payments in lieu of a standard annuity. Optional annuities reduce the monthly annuity payable during the retiree's life but provide for a beneficiary to receive a monthly benefit after the retiree's death, either for life or for a guaranteed period of time. The retiree may select one of three optional forms of payment that reduces the standard annuity based on age-related actuarial reduction factors.

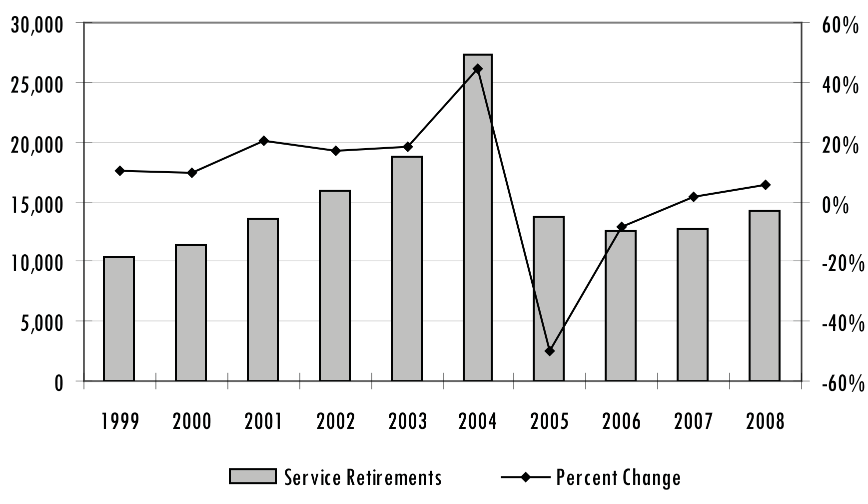
Retirees may also be eligible for early-age retirement. A member who became a member of TRS prior to September 1, 2007 and maintained membership until retirement becomes eligible if the member's age and years of credited service is less than 80 and reaches age 55 with 5 or more years of service credit or any age below 50 with 30 or more years of service credit.

Members who established TRS membership on or after September 1, 2007 are subject to new eligibility requirements. A new member will have a 5 percent reduction for each year under age 60 if the member retires with 30 years of service credit but does not meet the Rule of 80 at retirement, or the member retires before age 60 but the member's age and service credit total 80. Early-age service retirement annuity calculations are based on age, years of service credit at retirement, and when membership was established.

RETIREMENT BENEFITS

The TRS retirement plan is a defined benefit plan, meaning that the amount of a member's benefit is determined under a formula established by law and is not limited by the amount of the member's contributions to his/her retirement account. Members who meet the normal-age service requirements are entitled to receive a payment of a lifetime monthly annuity. **Figure 17** shows annual TRS service retirements since 1999. Although the percentage increase in the number of service retirements fluctuates from year to year, the data show a general upward trend in retirement rates until fiscal year 2005 and then a flattening or decrease in the trend in subsequent years.

FIGURE 17
ANNUAL SERVICE RETIREMENTS AND ANNUAL PERCENTAGE CHANGE IN NUMBER OF RETIREMENTS, 1999 TO 2008



Source: Teacher Retirement System.

DISABILITY RETIREMENT

A member, regardless of age or years of service credit, may receive a disability retirement if the member is mentally or physically disabled from the further performance of his or her duty and if the member's disability is probably permanent.

The member's disability is certified by the TRS Medical Board. A member who qualifies for disability retirement and has at least 10 years of service credit is entitled to a monthly annuity that is not reduced due to early age. The member may select a standard annuity or one of five optional annuities. If the member selects an optional annuity plan, the member's monthly annuity will be reduced by using disability retirement actuarial factors to reflect the additional liability for payment to the member's beneficiary.

A member who qualifies for disability retirement but has less than 10 years of service credit is entitled to a monthly disability benefit of $150 that is paid for the lesser of (1) the number of months the member has been covered by TRS, (2) the duration of the member's disability, or (3) the duration of the member's life. Legislation passed during the Eightieth Legislature, 2007, requires disability retirees to file an annual compensation statement with TRS and may forfeit their disability annuity or have to pay an increased amount for TRS-Care coverage if earned compensation exceeds the limits set by the TRS Board of Trustees. The new requirement does not apply to members who applied for disability prior to September 1, 2007 or whose effective date of disability retirement is prior to September 1, 2007.

PROPORTIONATE RETIREMENT

A member who has active membership credit in more than one Texas public statewide retirement system may be eligible to combine all of his or her service credit to satisfy eligibility requirements to retire under TRS. Retirement systems currently participating in the proportionate retirement program are:

- Teacher Retirement System of Texas (TRS);
- Employees Retirement System of Texas (ERS);
- Judicial Retirement System of Texas (Plans One and Two);
- Texas Municipal Retirement System (TMRS);
- Texas County and District Retirement System (TCDRS);
- City of Austin Employees Retirement System;
- El Paso City Employees' Pension Fund; and
- El Paso Firemen and Policemen's Pension Fund.

DEATH BENEFITS FOR ACTIVE EMPLOYEES

The primary beneficiary of an active member has five options to elect in the event of the member's death before retirement and if the member dies in a school year in which the member has performed TRS-covered service. Benefit options include a lump sum payment, 60 monthly payments, or a combination of lump sum payment plus a monthly benefit. The benefits are also available when a member is absent from service, such as when the absence is due to a sickness or accident or other work absences as described by law.

DEATH BENEFITS FOR RETIREES

The designated beneficiary of a service or disability retiree is entitled to receive a lump sum death and survivor benefit payment of $10,000 in addition to any joint and survivor or guaranteed period annuity that may be payable under an optional plan chosen by the retiree at retirement, unless the retiree has exhausted all monthly payments before death. In lieu of the $10,000 death and survivor benefit, eligible survivors may select alternative payment options, which include a lump sum payment of $2,500 and an applicable monthly survivor benefit payment

OPTIONAL RETIREMENT PROGRAM (ORP)

The Optional Retirement Program (ORP) is a defined contribution plan created in 1967 as a more portable alternative to the Teacher Retirement System and serves as a recruitment tool to draw higher education faculty, librarians, and certain professionals and administrators that require interstate mobility during their careers. The Texas Higher Education Coordinating Board and the governing board of each individual institution of higher education administer an Optional Retirement Program that is available to certain higher education employees as an alternative to participating in the Teacher Retirement System.

New ORP-eligible employees are automatically enrolled in the Teacher Retirement System (TRS) unless election to participate in the ORP is made. This election is a one-time, irrevocable choice between the ORP and TRS and must be made within 90 days of first becoming eligible. Participation in the program is limited to full-time faculty and certain administrators employed by Texas public institutions of higher education (including public community and technical colleges), the commissioners of education and higher education, and certain positions designated by law.

ORP is funded by tax-deferred contributions made by both the state and the employee. Employee and state contribution rates are established each biennium by the Texas Legislature and may fluctuate over time. The current active member contribution rate is set at 6.65 percent. The ORP state contribution rate is currently the same as the TRS rate, 6.58 percent. Institutions of higher education may provide supplements to the state rate, under certain conditions, up to 8.50 percent of payroll. State contributions are vested after one year of participation. ORP participants who terminate prior to meeting the vesting requirement forfeit state contributions made during that employment period. (See **Figure 18**.)

The ORP participant's benefit amount is directly dependent on the actual amounts contributed. Because the defined contribution plan allows each participant to manage their own personal investment accounts, there are no state provisions for improvement of benefits after termination (e.g., cost-of-living adjustments). Program participants purchase from insurance and investment companies individual investment contracts authorized under Internal Revenue Code Section 403(b). Vendor selection must be made from the employer's authorized list at the same time that ORP is elected. ORP participants assume full responsibility for monitoring their selected companies and investments.

Contributions and interest earnings are not subject to federal income tax until the funds are withdrawn or paid as a retirement annuity. Funds in the ORP accounts (including employee contributions) are available at termination of participation or when the member reaches age 70½. Termination of participating members occurs upon death, upon termination of employment in all Texas public institutions of higher education, or upon retirement.

INSURANCE

EMPLOYEES RETIREMENT SYSTEM

HISTORY

In 1975, the Legislature created the Texas Employees Uniform Group Insurance Program (UGIP) to provide high-quality health insurance and other option coverage for employees, retirees, and their eligible dependents beginning September 1, 1976. The program started as an indemnity health plan defined and administered by the Texas Group Benefits Act, Chapter 1551, Texas Insurance Code. Health Maintenance Organizations (HMOs) at that time provided health services to participants who chose to use them. Now known as the Group Benefits Program (GBP), it has grown over the years and now also offers health insurance coverage to most institutions of higher education, except The University of Texas and Texas A&M University, which administer their own programs.

PROGRAM BENEFITS

Health and other insurance benefits for employees and retirees are subject to change based on available state funding. The GBP offers two types of health insurance plans: HealthSelect and health maintenance organizations (HMOs). Both provide comprehensive health and prescription drug benefits, but there are some differences in the way benefits work. Unlike HealthSelect, which is available in all Texas counties, HMOs provide services by county, and employees can enroll in an HMO if they live or work in a county served by one of the HMOs in the program.

HealthSelect, the self-funded plan that is currently in use, was introduced on September 1, 1992. Higher education employees who were not part of The University of Texas or Texas A&M University systems were added to the health plan at the same time. The Legislature added Community Supervision and Corrections Department employees on September 1, 2004.

FIGURE 18
OPTIONAL RETIREMENT PROGRAM APPROPRIATION AND MEMBERSHIP HISTORY
(IN MILLIONS)
FISCAL YEARS 2006 TO 2009

	2006	PERCENTAGE CHANGE	2007	PERCENTAGE CHANGE	2008	PERCENTAGE CHANGE	2009	PERCENTAGE CHANGE
Appropriation	$124.3	6.20	$126.7	1.91	$140.6	11.04	$144.9	3.00
Membership	38,115	1.90	39,429	3.40	40,191	1.90	40,222	1.00

SOURCE: Texas Higher Education Coordinating Board.

In addition to health insurance and accompanying prescription drug program, there also are the following optional coverage programs offered: Dental, Term Life Insurance, Voluntary Accidental Death & Dismemberment, Long-term and Short-term Disability, and Long-term Care. The Legislature introduced a Flexible Spending Account, now known as a Health Care Reimbursement Account (TexFlex), for state employees on September 1, 1988. TexFlex gives employees the opportunity to fund accounts for themselves and their dependents with payroll deductions that reduce federal income and Social Security taxes. State workers may contribute a minimum of $15 a month to a maximum of $416 a month. TexFlex will reimburse medical, dental, and vision expenses such as copays, deductibles, coinsurance, and other costs that exceed the health plan benefit. Historically, the Legislature has not appropriated funds for the program; it was created to operate on participant fees.

ERS has two dental plans available to employees and retirees, the Dental HMO, and the State of Texas Dental Choice Plan. The Dental HMO works like an HMO and members and their eligible dependents must get their dental care within the Dental HMO service area. The Dental Choice Plan allows members to visit any dentist, and they and their eligible dependents can enroll regardless of where they live.

Basic Term Life insurance coverage is included with GBP health coverage. An employee receives a $5,000 policy, and a retiree receives a $2,500 policy. Employees can also sign up for group term life insurance coverage worth one times their annual salary or two times their annual salary without proof of good health. With evidence of insurability, employees can sign up for life insurance coverage worth three times their annual salary or four times their annual salary at any time. Retirees may continue the coverage they had as an employee or sign up for a $10,000 policy.

Dependent Term Life insurance coverage is also available in the GBP. Dependent Term Life insurance provides life insurance coverage for each covered family member and requires a monthly premium. An employee is eligible to sign up for a $5,000 policy, and a retiree is eligible to sign up for a $2,500 policy.

Voluntary Accidental Death & Dismemberment (AD&D) coverage is available in the GBP. Voluntary AD&D provides benefits in the event of an accident or certain accidental injuries, is in addition to AD&D benefits provided with Basic and Optional Term Life for active employees, and requires a monthly premium.

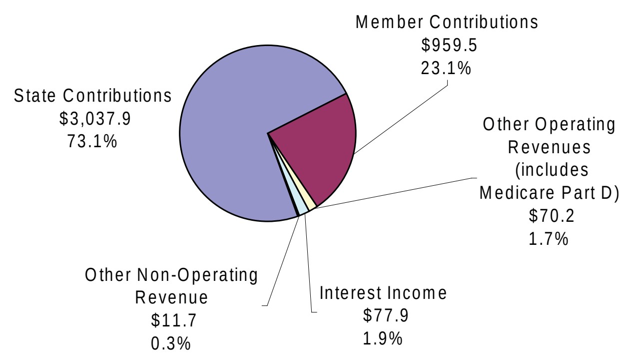
Both Short-term and Long-term Disability insurance is available in the GBP. The Short-term Disability benefit provides a portion of an employee's monthly salary if illness or injury keeps him or her from working. To be eligible for benefits, a physician must certify the employee as totally disabled. Benefits are paid for a period of up to five months. The Long-term Disability benefit works the same way except the length of time the employee receives benefit payments depends on the employee's age at the onset of the disability.

Long-term care insurance is available for state employees, retirees, and certain family members. This insurance provides certain benefits not covered by the medical plan, such as nursing home care and adult day care. An employee's family members can apply for coverage, even if the employee does not.

STATE FUNDING/APPROPRIATIONS

HealthSelect and HMO premiums are funded by a combination of sources: state contributions, member contributions, local funds from participating entities, and investment earnings. **Figure 19** summarizes the GBP funding sources for the 2008–09 biennium. The GBP reserve fund, which will have a projected balance of $260 million at the end of fiscal year 2009, is also used to cover health benefit cost increases. The state pays 100 percent of the premium for full-time employees and 50 percent of dependent coverage; members pay the other 50 percent of the dependent coverage. For part-time employees and graduate teaching assistants, both the state and the member contribute 50 percent. For

FIGURE 19
ERS GROUP BENEFITS PROGRAM FUND SOURCES 2008–09 BIENNIUM
(IN MILLIONS)



Source: Employees Retirement System.

those members' dependents, the state contributes 25 percent.

The Legislature appropriates funds for the state contribution at the end of each article for general state agencies as an estimated appropriation. The total appropriation for all state agencies is shown as an informational listing in the ERS appropriation pattern. Higher education institutions receive a sum-certain appropriation for insurance and must supplement any shortages with local funds.

TEACHER RETIREMENT SYSTEM – HEALTH BENEFIT PLANS

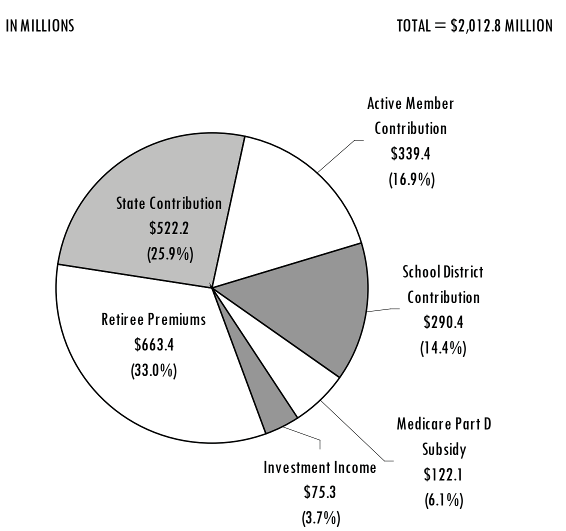
TRS-CARE (RETIREE HEALTH INSURANCE)

In 1985, the Legislature authorized the establishment of the Texas Public School Retirement Employee Group Insurance Program (TRS-Care) and designated the Teacher Retirement System as its administering agency. The program is established through Chapter 1575 of the Texas Insurance Code and through Title 34, Part 3, Chapter 41 of the Texas Administrative Code and is separate from any program providing health care benefits to actively employed public school employees.

FUNDING

TRS-Care has six major revenue sources: current retirees, current active employees, local school districts, state contributions, Medicare Part D subsidies, and investment income. **Figure 20** summarizes the funding sources for the 2008–09 biennium. As of the August 31, 2008 actuarial valuation, retiree premiums accounted for approximately 37.6 percent of expected claims and expense costs. Active members contribute at a rate of 0.65 percent of payroll and local school districts at a rate of 0.55 percent of payroll. Appropriations for the 2008–09 biennium total $452.3 million in General Revenue funds and meet the statutory requirement that the state contribute an amount equal to 1 percent of public education payroll. At the close of fiscal year 2008, the TRS-Care trust fund balance reflects a positive balance of $729 million, which indicates that contributions exceeded the annual expected claims payments. The asset fund balance of $729 million represents more than one year of employer-provided benefits.

FIGURE 20
TRS-CARE PROJECTED FUNDING SOURCES
2008–09 BIENNIUM



SOURCE: Teacher Retirement System.

ELIGIBILITY

To be eligible for TRS-Care, retirees must have at least 10 years of TRS service credit, which may include up to 5 years of military service credit but may not include any other special or equivalent service credit purchased. Additionally, the member must meet one of the following requirements:

- The sum of the retiree's age and years of service credit in TRS equals or exceeds 80 at the time of retirement, regardless of whether the retiree had a reduction in the retirement annuity for early age (years of service credit can include all purchased service); or
- The retiree has 30 or more years of service credit in TRS at the time of retirement (years of service credit can include all purchased service).
- Disability retirees are initially eligible for TRS-Care regardless of the number of years of service credit. TRS-Care coverage for disability retirees with less than 10 years of TRS service credit ends when the disability retirement benefit ends.

Health benefits are provided for public school retirees who are not eligible to participate in the state higher education or state employee plans. Basic coverage is available to retirees at no cost but retirees must contribute toward any additional cost in excess of base coverage. Members must also contribute towards the cost of spouse and dependent children coverage. **Figure 21** summarizes the benefit levels provided under the three tiers of coverage from September 1, 2008 through August 31, 2009:

COVERAGE

As depicted in **Figure 21**, TRS-Care consists of three tiers of coverage: TRS-Care 1, TRS-Care 2, and TRS-Care 3. Each

FIGURE 21
TRS-CARE BENEFIT LEVELS, FISCAL YEAR 2009

	TRS-CARE 1			TRS-CARE 2	TRS-CARE 3
	RETIREES OR SURVIVING SPOUSES ENROLLED IN MEDICARE PART A AND ELIGIBLE FOR PART B	RETIREES OR SURVIVING SPOUSES NOT ENROLLED IN MEDICARE PART A AND ELIGIBLE FOR PART B	RETIREES OR SURVIVING SPOUSES NOT ELIGIBLE FOR MEDICARE	ALL	ALL
Deductible	$1,800	$3,000	$4,000	$1,000	$300
Family Deductible	$3,600	$6,000	$8,000	$2,000	$600
Coinsurance Limit	$3,000	$3,000	$3,000	$3,000	$3,000
Family Coinsurance Limit	$6,000	$6,000	$6,000	$6,000	$6,000
Maximum Out-of-Pocket	$4,800	$6,000	$7,000	$4,000	$3,300
Family Maximum Out-of-Pocket	$9,600	$12,000	$14,000	$8,000	$6,600

NOTE: Lifetime maximum: unlimited.
SOURCE: Teacher Retirement System.

tier has deductibles or premiums that are differentiated by the retiree's or surviving spouse's Medicare status. Dependents must be enrolled in the same coverage tier as the retiree or surviving spouse.

TRS-Care 1 is a self-funded plan providing basic catastrophic coverage, with a $1,800, $3,000, or $4,000 deductible based on the retiree's Medicare status.

TRS-Care 2 is a self-funded comprehensive plan with a $1,000 deductible, $35 in-network physician office visit copay, and a separate prescription drug plan with various copays.

TRS-Care 3 is a self-funded comprehensive plan with a $300 deductible, $25 in-network physician office visit copay, and a separate prescription drug plan with various copays.

Aetna Life Insurance Company administers TRS-Care medical benefits and Caremark administers pharmacy benefits. The TRS-Care health benefit plan offers comprehensive health care through statewide and nationwide networks of hospitals, physicians, and other health care providers and pharmacies. Participants who use network providers are generally reimbursed for 80 percent of eligible expenses after satisfying a deductible each plan year. Services provided out-of-network are reimbursed at a lower rate.

ACTIVE EMPLOYEES (TRS-ACTIVECARE)

TRS-ActiveCare is a self-insured plan established by the Seventy-seventh Legislature, 2001. The statewide healthcare coverage program went into effect on September 1, 2002 and provides health benefits for employees of school districts, open enrollment charter schools, regional education service centers, and other educational districts whose employees are members of the Teacher Retirement System. Of the 1,360 districts/entities eligible to participate in TRS-ActiveCare, over 346,000 employees and dependents from 1,081 entities have elected to participate. (See **Figure 22**.)

FIGURE 22
TRS-ACTIVECARE MEMBERSHIP AS OF AUGUST 31, 2008

Districts/Entities	1,081
Employees	206,908
Dependents	138,940
TOTAL PARTICIPANTS	**345,848**

SOURCE: Teacher Retirement System.

The state does not contribute to the cost of premiums for active employee health coverage. TRS active employees pay premiums into a separate fund from which health claims are paid. To participate, an employee must be employed by a participating entity and must be an active contributing TRS member or must be employed for 10 or more hours per week.

Blue Cross and Blue Shield of Texas administers the medical benefits and Medco Health Solutions administers pharmacy benefits. TRS-ActiveCare also offers a choice of three preferred provider organization (PPO) plans statewide. Additionally, health maintenance organizations are available in certain service areas.

HIGHER EDUCATION GROUP INSURANCE

HISTORY, STRUCTURE, AND ENROLLMENT

In the early 1990s higher education institutions were given the option of joining ERS' Uniform Group Insurance Program (or UGIP, and now called the Group Benefits Program). All institutions of higher education opted to join UGIP, except The University of Texas and Texas A&M University Systems, which opted to continue operating separate health insurance programs for their respective systems.

Higher Education Group Insurance (HEGI) provides state contributions for health insurance premiums for employees and dependents of institutions of higher education. These contributions are appropriated in Article III of the General Appropriations Act under the bill pattern entitled, "Higher Education Employees Group Insurance Contributions."

HEGI contributions are made to three systems: the Employees Retirement System, The University of Texas System (UT) and the Texas A&M University System (A&M). The higher education employees insured by ERS participate in the Group Benefits Plan, while both The University of Texas and Texas A&M University Systems administer their own plans based on criteria germane to each system.

Figure 23 shows the number of state-funded higher education enrollees (excluding dependents) in each of the three systems.

Furthermore, higher education employees are enrolled in several types of higher education institutions. **Figure 24** shows the plurality of higher education institution enrollees working for general academic institutions, although community colleges also compose a large portion of total enrollment, despite being local (i.e., non-state) employees.

FUNDING AND PROPORTIONALITY

The HEGI appropriation is intended to help institutions cover the cost of health insurance premiums for institution employees whose salaries are paid from the General Revenue Fund. Because The University of Texas and Texas A&M University Systems operate their own health insurance programs, they each receive separate appropriations. The remaining institutions are included in the program operated by the Employees Retirement System (ERS).

For the 2008–09 biennium, the allocation of General Revenue Funds is based on the relative number of employees at the institution enrolled in the health insurance program as of December 1, 2006. Funding is based on a sum-certain appropriations methodology in which state contributions are capped at the respective institution's line-item amount and

FIGURE 23
NUMBER OF STATE-FUNDED HIGHER EDUCATION ENROLLEES, 2000–2008 (EST.)

	2000	2002	2004	2006	2008, EST.
ERS	54,356	59,307	56,442	56,980	45,185
UTS	34,229	34,048	33,034	32,255	32,559
TAMUS	17,162	17,390	16,296	15,532	16,541
TOTAL	**105,747**	**110,745**	**105,772**	**104,767**	**94,285**

Source: Legislative Budget Board.

FIGURE 24
STATE-FUNDED HIGHER EDUCATION ENROLLMENT BY TYPE OF INSTITUTION, 2000–2008 (EST.)

	2000	2002	2004	2006	2008 (EST.)
Community Colleges	29,541	32,666	30,716	32,574	19,706
General Academic Institutions	46,809	49,668	46,959	45,538	46,716
Health-related Institutions	22,732	21,413	21,303	20,154	21,062
Texas A&M System Agencies	4,513	4,676	4,405	4,069	4,208
Texas State Technical Colleges	1,591	1,726	1,725	1,564	1,662
Two-Year Lamar State Colleges	426	477	483	517	467
System Offices	135	119	181	351	464
TOTAL	**105,747**	**110,745**	**105,772**	**104,767**	**94,285**

Source: Legislative Budget Board.

where additional costs, if any, must be borne by individual institutions out of other appropriated or local funds.

Appropriations for HEGI are intended to provide state contributions to individual institutions' costs of health insurance premiums in a manner prescribed by proportional cost-sharing requirements. As such, institutions are required to pay all the health benefit costs for those employees having their salaries paid from sources other than the General Revenue Fund. Thus, as institutions continue to increase their share of funding from sources other than General Revenue Funds, the share of employees having their health benefits paid by the state decreases proportionately.

One result of the requirement for proportional cost-sharing is that the overall share of the total health insurance enrollment paid from funds other than General Revenue Funds has increased over time. **Figure 25** shows this trend since 2000.

Figure 26 provides detail on the state general revenue dollars appropriated to the three systems over time. The fiscal year 2009 community college contribution was vetoed and is not included in **Figure 26**.

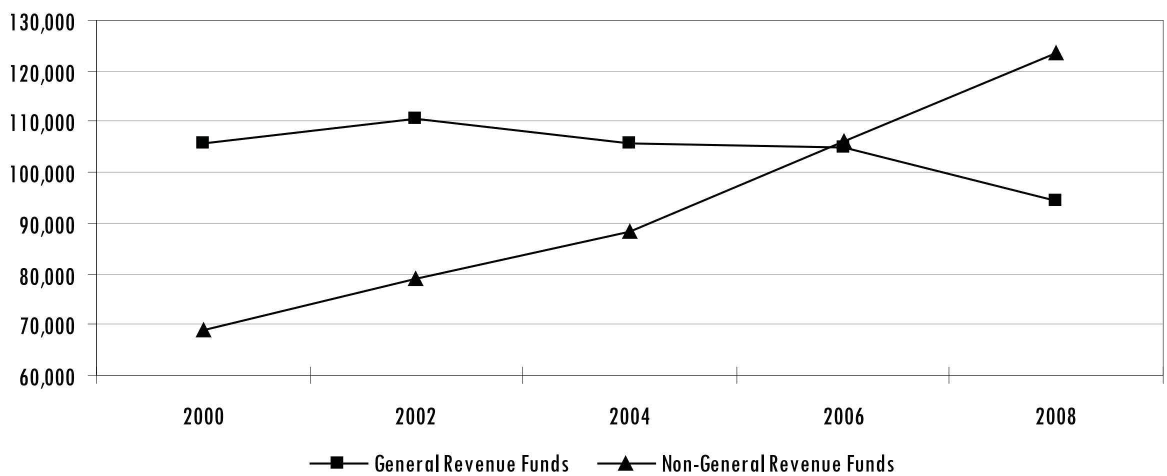
Legislative appropriations for HEGI for the 2008–09 biennium total $853.0 million, of which $851.8 million is in General Revenue Funds and $1.1 million is in Other Funds. The appropriation is $90.0 million in All Funds less than the 2006–07 biennium level, which is partly attributable to the Governor's veto of $154 million in the fiscal year 2009 group insurance line-item for public community colleges. Prior to this veto, the 2008–09 All Funds HEGI appropriation was $1,007.0 million, or about $64.0 million above the 2006–07 biennium level.

However, the legislative leadership and the Governor reached a tentative agreement to restore the vetoed group health insurance funds to community colleges. Under this agreement, in fiscal year 2009, community colleges will receive $99 million in group health insurance funding and an additional $55 million in one-time transitional funding. The transitional funding is intended to ease the shift toward providing state contributions only for individuals whose salaries are directly supported by state funds.

The Legislature provided $1.5 million in General Revenue Funds to continue funding the higher education portion of the state's contributions for the State Kids Insurance Program. The Legislature also provided $1.1 million in State Highway Funds for the Texas Transportation Institute (TTI).

The HEGI appropriation is sum-certain. That is, the state's current General Revenue contributions are limited to each institution's number of employees enrolled in the health insurance program as of December 1, 2006. However, the General Appropriations Act allows ERS and The University of Texas and Texas A&M University Systems to transfer HEGI appropriations among institutions within their respective group insurance programs to address shortfalls in General Revenue funding related to group insurance premiums.

FIGURE 25
GENERAL REVENUE AND NON-GENERAL REVENUE GROUP INSURANCE HEADCOUNT
2000–2008



SOURCE: Legislative Budget Board.

FIGURE 26
2008–09 GENERAL REVENUE FUND DOLLARS

	2008–09 GENERAL REVENUE FUND DOLLARS
General Academic Institutions	$416,747,750
Community Colleges	159,028,717
Texas State Technical Colleges	16,778,692
Health-related Institutions	204,371,946
System Offices	3,481,182
Two-Year Lamar State Colleges	5,332,642
Texas A&M System Agencies	45,771,780
State Kids Insurance Program	1,451,522
TOTAL	**$852,964,231**

Source: Legislative Budget Board.

Like general academic and health-related institutions, community colleges receive General Revenue Fund contributions for group insurance. However, since community college employees are local, state contributions for health benefits are fully discretionary. Other agencies and institutions of higher education report employee eligibility for General Revenue-funded group health insurance benefits only if the employee's salary is directly paid with General Revenue Funds.

However, in the past, community colleges tended to base eligibility for General Revenue-funded benefits if the employee's job function fell under an approved "element of cost." This practice caused community colleges to report eligibility for state-funded health benefits in a manner that did not consistently match the source of the employee's salary.

This practice led to the Governor's veto of the community colleges' fiscal year 2009 Group Health Insurance appropriation ($154 million). However, an agreement to proportionalize community college group health insurance appropriations for the 2010–11 biennium led to an agreement to restore the vetoed funds during the Eighty-first Legislative session in January of 2009.

PLAN OPTIONS/OVERVIEW

Because ERS-covered institutions are insured within the GBP, the insurance contribution policy for ERS-covered institutions is the same as for non-higher education general state employees. For full-time employees, the state pays the employee-only premium in full and half the difference between the employee-only premium and the premium for dependent coverage. For full-time employees of The University of Texas System, the state also pays the employee only premium in full and half the difference between the employee-only premium and the premium for dependent coverage. For full-time employees of the Texas A&M University System, the state pays about 86 percent of the employee-only premium and half of the difference between the employee-only premium and the premium for dependent coverage. Employees of The University of Texas and Texas A&M University Systems receive an array of benefits similar to those offered by ERS.

GLOSSARY

Actuarial Accrued Liabilities	That portion, as determined by a particular actuarial cost method, of the actuarial present value of the plan benefits and expenses which is not provided for by future normal costs.
Actuarial Soundness	A public retirement system is considered actuarially sound if an actuary determines that the fund has sufficient money to pay ongoing normal cost and amortize the Unfunded Actuarial Accrued Liability over a period of time not to exceed 40 years, preferably 25 to 30 years.
Annually Required Contribution (ARC)	The ARC is the normal cost plus the portion of the unfunded actuarial accrued liability to be amortized in the current period.
Defined Benefits	In a retirement plan, benefits which are defined by a specific formula applied to a specific member compensation and/or specific years of service. The amount of the benefit is not a function of contributions or actual earnings on those contributions.
Defined Contributions	A system providing pension benefits equal to the combined employer and employee contributions plus interest and minus administrative expenses.
Experience Study	A periodic review and analysis of the actual experience of the system which may lead to a revision of one or more actuarial assumptions.
Normal Cost	The annual cost assigned, under the actuarial funding method, to current and subsequent plan years. It is expressed as a percent of pay and is equal to the present value at hire of all possible benefits of the system divided by the present value of anticipated future compensation to be received by the new member.
Unfunded Actuarial Accrued Liability (UAAL)	The difference between the actuarial accrued liability and valuation assets. Sometimes referred to as “unfunded accrued liability.”
Copayment	The cost-sharing arrangement in which a member of a managed healthcare plan pays a fixed dollar amount for a service.
Children’s Health Insurance Program (CHIP)	The Children’s Health Insurance Program is a national program designed for families who earn too much money to qualify for Medicaid, yet cannot afford commercial insurance. The State of Texas offers a benefits package with a range of coverage including regular check-ups, immunizations, prescription drugs, eyeglasses, lab tests, X-rays, hospital visits, dental care, and mental care.
Proportionality	A funding mechanism establishing the share of a benefit’s total cost borne by the state of Texas and a given agency. Proportionality requires state General Revenue Fund benefits contributions be paid only on salaries also paid with state General Revenue Fund.
State Kids Insurance Program (SKIP)	Very similar to CHIP, the State Kids Insurance Program (SKIP) was started in 1999 by the Texas Legislature to help children of State of Texas employees have access to more affordable health care. SKIP is available to children of employees in ERS’ insurance program, the Texas Employees Group Benefits Program (GBP).
Sum-certain Funding	A funding mechanism setting the state’s contribution for higher education group health insurance at certain levels. Any costs incurred over these levels must be borne by the institutions.

SOURCES: Legislative Budget Board; Teacher Retirement System; Pension Review Board; Employees Retirement System.