Does Senate Bill 321 Meet the Objectives for Good Pension Reform?

reason FOUNDATION

Objectives	Status Quo	SB 321
Keeping Promises *Ensure the ability to pay 100% of the benefits earned and accrued by active workers and retirees*	NO	YES
Retirement Security *Provide retirement security for all current and future employees*	FOR SOME	YES
Predictability *Stabilize contribution rates for the long-term*	NO	YES
Risk Reduction *Reduce pension system exposure to financial risk and market volatility*	NO	YES
Affordability *Reduce long-term costs for employers, employees*	NO	YES
Attractive Benefits *Ensure the ability to recruit 21st Century employees*	NO	YES
Good Governance *Adopt best practices for board organization, investment management, and financial reporting*	SOME	N.A.

2021 Texas Senate Bill 321 Analysis
by the Pension Integrity Project at Reason Foundation

Leonard Gilroy, Sr. Managing Director (leonard.gilroy@reason.org)
Steven Gassenberger, Policy Analyst (steven.gassenberger@reason.org)

Objectives	Status Quo	SB 321
Keeping Promises	The Employees Retirement System of Texas (ERS) is nearly $15 billion short of the funds needed today to ensure promised benefits are paid in the future. ERS is forecasted to exhaust its assets completely by 2061 if all current actuarial assumptions hold.	Adopting a funding policy based on actuarially determined contribution rates guarantees the state fully funds all earned ERS benefits regardless of market performance and helps the state avoid accruing unfunded liabilities into the future.
Retirement Security	While ERS pension benefits are legally protected, structural underfunding and other factors have led to rapidly growing ERS pension debt. Absent reforms, ERS is projected to become insolvent in the coming decades, meaning the state's ability to ensure its members' retirement security faces long-term risk.	SB321 eliminates structural underfunding by ensuring that future rates align with actuarial recommendations designed to steer ERS toward a path to full funding and long-term solvency.
Predictability	Contribution rates today may be considered *technically* predictable because they are fixed in statute, but this has also lead to structural underfunding and increases in unfunded liabilities, resulting in highly variable and unexpected cost volatility over time.	Long-term budget predictability and predictability about contribution rates are two very different things. The historical focus on the latter has made the former unachievable. SB 321 exchanges the false predictability of today's fixed, but insufficient, ERS contributions with the true predictability of a policy designed to pay off ERS unfunded liabilities completely, on a fixed scheduled with a certain end date.
Risk Reduction	The current assumed return of 7% has about a 28% probability of being achieved on average over the next 10 years. Without a shift in expectations, ERS is still practically guaranteed to accrue pension debt due to structural underfunding and weak investment returns.	Increasing contributions is a critical step towards long-term solvency, but additional future steps may be needed to address the overall financial risk in the legacy ERS pension plan. The legacy ERS plan will continue to face market volatility, a lower-yield investment climate, and an assumed rate of return and discount rate that are likely higher than economic conditions would warrant. Future adjustments to actuarial assumptions will likely be needed.
Affordability	ERS unfunded liabilities generate major long-term costs through interest on the pension debt, creating unfunded liabilities that in turn drive fiscal pressures for employers.	The cash balance plan for new hires will provide a predictable, affordable means of controlling employer retirement costs over the long term. However, SB 321 will result in additional *near-term* contributions in exchange for approximately $15 billion in long-term savings.
Attractive Benefits	The current ERS pension disproportionally benefits those who stay for a full 28 years of service (unreduced retirement benefit), which only 14% of newly hired state employees achieve.	Given nearly 64% of all new hires are likely to leave their public employer before initially vesting, SB 321 meets the retirement security needs of members more equitably, by offering a guaranteed benefit with enhanced portability for an increasingly mobile professional workforce.
Good Governance	ERS generally is a well operated enterprise delivering high quality services. However, there is opportunity to increase transparency and reporting regarding the system's growing investment portfolio of limited private partnerships.	SB 321 does not address the plan's governing structure.

Leonard Gilroy, Sr. Managing Director (leonard.gilroy@reason.org)
Steven Gassenberger, Policy Analyst (steven.gassenberger@reason.org)