ACCOUNTING FOR LAW ENFORCEMENT/ CUSTODIAL OFFICER RETIREMENT COSTS

Based on the August 31, 2016 Actuarial Valuations

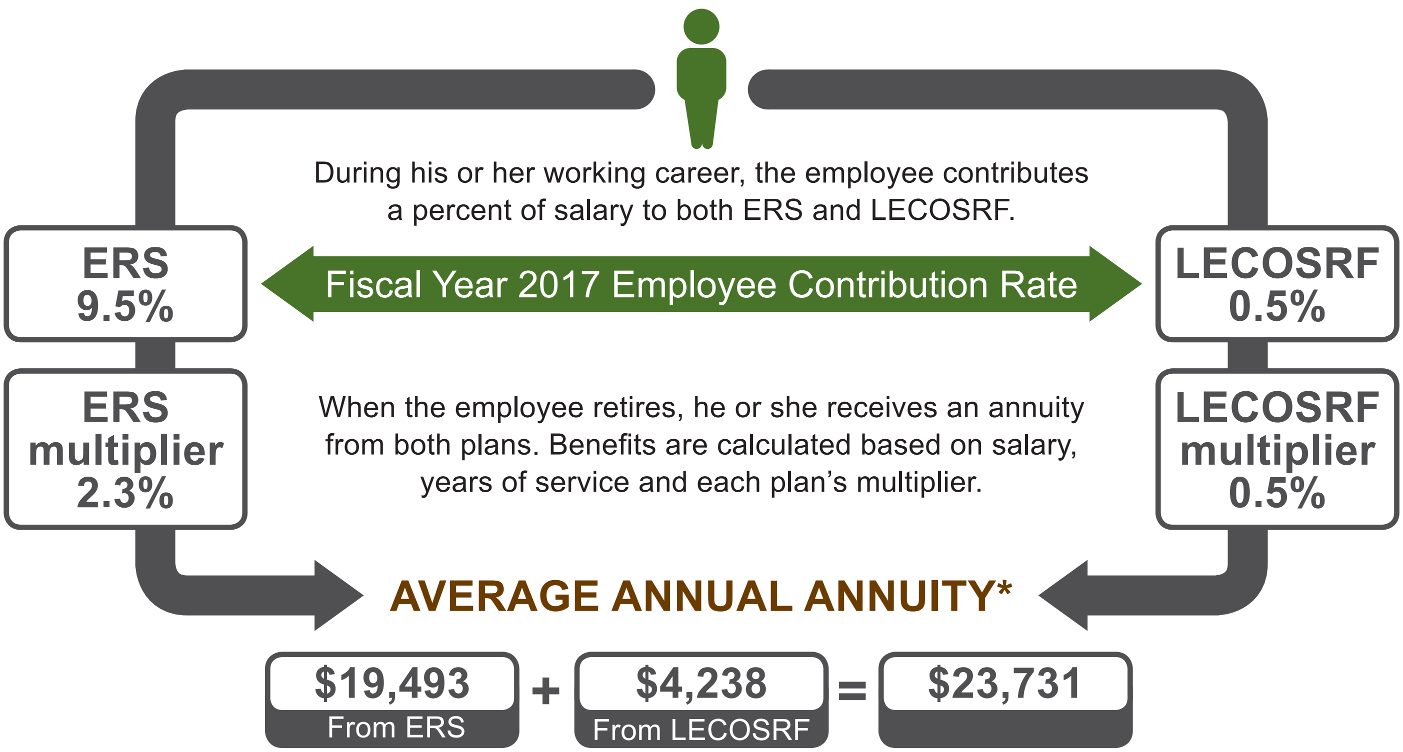
ERS Employees Retirement System of Texas

ISSUE: Law Enforcement and Custodial Officers (LECO) have higher cost benefits that increase funding requirements for the state's retirement plans.

Pension plans such as the ones administered by ERS are based on years of service, final average salary and a benefit multiplier. LECO employees and Regular Class state employees both receive annuities from the ERS Retirement Trust Fund, which includes a 2.3% benefit multiplier.

In addition, LECO employees receive supplemental retirement benefits from a separate trust fund called the Law Enforcement and Custodial Officers Supplemental Retirement Fund (LECOSRF), which offers an additional 0.5% benefit multiplier. The ERS Retirement Trust Fund pays about 82% of the LECO's retirement benefit .

A LECOSRF-eligible member will receive a benefit from the ERS and LECOSRF plans.



For the average LECOSRF retiree, about 82% of his or her annuity is from the ERS plan and about 18% is from LECOSRF.

*Based on August 31, 2016 valuation (most recent available)

LECO benefits cost more than those provided to other Regular Class state employees, because law enforcement and custodial officers can retire younger with fewer years of service. Despite the difference in costs, the two groups contribute the same percentage to the ERS plan, currently 9.5% for Fiscal Year 2017. LECO employees have also been contributing 0.5% of payroll since Fiscal Year 2010 for the supplemental benefit from LECOSRF.

In general, LECO employees receive a more expensive retirement benefit than Regular Class employees including:

- the ability to retire at a younger age with a full, unreduced annuity from both the ERS main fund and LECOSRF;
- an annuity from the main ERS fund that is about 10% more valuable than what Regular Class employees receive; and
- a combined ERS and supplemental annuity that's 25% more valuable.

Demographic trends among the two populations also highlight this benefit trend. As shown in the table on page 2, LECO members, compared to Regular Class members, retire from state employement at a younger age, with fewer years of service and receive a higher benefit. LECO employees are younger, have fewer years of service and make a lower salary than Regular Class state employees.

Key Demographics for Regular Class and LECO Populations* – As of August 31, 2016

Average Regular Class Retiree	
Average Annuity	$19,547
Years of Service	22.4
Age Currently	69.5
Age at Retirement	59.0
Average Regular Class Employee	
Average Annual Salary	$47,173
Years of Service	8.8
Age Currently	44.2
Age When Hired	35.4

Average LECO Retiree**	
Average Annuity	$23,731
Years of Service	21.7
Age Currently	64.1
Age at Retirement	55.3
Average LECO Employee	
Average Annual Salary	$44,634
Years of Service	8.0
Age Currently	41.0
Age When Hired	33.0

*Statistics shown for Regular Class retirees and employees are separate and distinct from statistics shown for LECO retirees and employees.
Annuitants with at least 10 years of Certified Peace Officer (CPO)/Custodial Officer (CO) service are identified as LECO annuitants. There are some annuitants who earned service as a CPO/CO who did not work long enough (20 years) to be eligible for a LECOSRF annuity, but do receive an ERS annuity. **Source: Gabriel Roeder Smith.

By the Numbers - Separating LECO Costs

How do the liabilities, assets and cost rates differ for LECO members?

Summary comparison of assets and liabilities by member population
As of August 31, 2016

	Regular Class State Employees	Law Enforcement & Custodial Officers
Membership		
Active members	107,324	39,066
Retirees and beneficiaries[1]	86,180	17,578
Inactive members, Vested	14,169	2,428
Inactive members, Non-vested	71,402	20,874
Total Membership	279,075	79,946
Valuation Payroll (billions)[2]	$5.1	$1.7
Contribution Rates		
Member[3]	9.50%	10.00%
Agency	0.50%	0.50%
State[4]	9.50%	10.0%
Total Contribution Rate	19.50%	20.50%
Actuarially Sound Contribution Rate (%)[4]	19.47%	23.38%
Contribution Rate Sufficiency *Negative figure indicates contribution shortfall*	0.03%	(2.88%)
Assets		
Market Value (billions)[2]	$20.0	$5.3
Actuarial Value (billions)[2]	$21.7	$5.8
Actuarial Information		
Normal Cost Rate (%)	12.11%	14.58%
Accrued Liability (billions)[2]	$28.0	$8.6
Unfunded Liability (billions)[2]	$6.3	$2.8
Funded Ratio (%)	77.5%	67.3%
Funding Period	31	Never

[1] Annuitants with at least 10 years of service as a Certified Peace Officer (CPO)/Custodial Officer (CO) shown as LECO annuitants.
[2] Number rounded.
[3] The LECO member contribution of 10.0% represents a 9.5% contribution to ERS and a 0.5% contribution to the LECOSRF Trust.
[4] The LECO state contribution of 10.0% represents a 9.5% contribution to the ERS trust and a 0.5% contribution to LECOSRF. The state contribution, and the resulting ASC rate, excludes the $19.2 million in court fees that are deposited to the LECOSRF. The court fees are not expressed as a percent of payroll.
Source: Gabriel Roeder Smith.

LECO members and retirees represent 22% of the total ERS/LECOSRF membership. The normal cost for LECO employees is 2.47% higher than Regular Class state employees. Ideally the total contributions received by the trusts would be at least that amount higher for LECO employees, to reflect the higher cost of their benefit accruals. With unfunded liabilities, LECO employees require a total contribution of 23.38%, which is 3.91% higher than Regular Class state employees.

One possibility is for the state to set contribution rates by member population rather than by plan.

Accounting separately for LECO and ERS members does not lower liabilities; it allocates costs more appropriately to each group. *Both the ERS and LECOSRF plans have been chronically underfunded. From fiscal years 1996 to 2017, in 21 out of 22 years ERS has not received the full contribution needed. The Legislature took a contribution holiday in LECOSRF from fiscal years 1994 through 2008. Since contributions resumed, full funding rates needed have not been met even though the state has increased the overall contribution rates.*