

LEGISLATURE FACES A TEXAS-SIZED BUDGET CRISIS

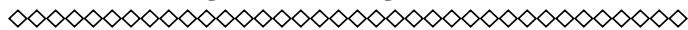
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Director of Government Relations

The 82nd Texas Legislature convened on Tuesday, January 11, for its 140-day Regular Session. Every legislative session has major challenges, but the impact of the state's multi-billion-dollar budget shortfall greatly overshadows every other issue this year. The size of the shortfall has been debated, with most estimates ranging from \$15 to \$27 billion. Any way you cut it, the state's budget crisis poses huge challenges to budget writers and creates serious threats for state employees and retirees. In order to enact a state budget within available revenue, legislators may eliminate thousands of state jobs, significantly reduce health benefits for active and retired employees, and cut or change retirement benefits.

State employees and retirees aren't alone in being threatened by the budget shortfall. Advocates for public education claim they are being underfunded by the base budget by \$9.8 billion. Proponents for Medicaid, higher education and other programs have similarly expressed concern about the impact of budget reductions. This has generated calls by many groups to utilize the state's \$9.4 billion "Rainy Day Fund", to raise taxes, or to otherwise avoid specific budget reductions.

TPEA staff will work closely with the leadership of both the House and Senate to try to mitigate employee layoffs, to maintain state employee and retiree health insurance benefits and to defend our retirement benefits. Everyone will feel the pain of this difficult budget cycle, but TPEA will work to make certain the burden of closing the budget shortfall is shared widely and equitably. We will continue to update you about the ongoing budget deliberations that will take place throughout the session.

Biennial Revenue Estimate and Magnitude of Budget Shortfall



The release of the Comptroller's Biennial Revenue Estimate (BRE) really kicks off the budget process. Comptroller Susan Combs released this session's Biennial Revenue Estimate on January 10, the day before the legislative session began. The BRE essentially tells lawmakers how much money they will have available for the next two year budget. The BRE projects that budget writers will have \$72.2 billion in general revenue for the 2012-2013 biennium, \$15 billion less than the \$87 billion in general revenue used in the current 2010-2011 budget. The BRE also estimates the budget deficit in the current biennium at \$4.3 billion, although this does not reflect some current year spending reductions.

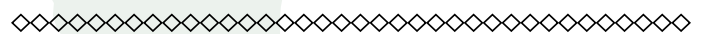
There has been debate about the size of the budget shortfall that Texas faces. In truth, the answer depends on how you define "shortfall". TPEA believes it is fair to say that on a revenue basis, the shortfall is around \$15 billion, the difference between available general revenue in the BRE and the amount used in the current 2010-2011 budget. Additionally, if the growth in costs to maintain current state services through the next biennium are included, the "current services" shortfall is in the range of \$27 billion. Most of the growth in current services costs are attributable to growth in student populations in public and higher education and increased health care costs resulting from caseload growth and medical inflation in Medicaid and other health programs.

HB 1 and the LBB 2011 Government Effectiveness and Efficiency Report



The final decisions about funding and budget cuts will be made in HB 1, the General Appropriations Act. The introduced version of HB 1 appropriates \$156.4 billion from all fund sources, which equates to a \$31 billion or 16.6 percent reduction from current 2010-2011 budget levels. In addition to HB 1, another influential document is the 2011 LBB Government Effectiveness and Efficiency Report, which contains a number of recommendations that could affect state employees and retirees.

State Workforce Reductions

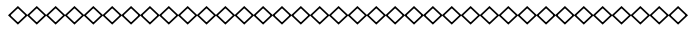


HB 1 shows a decrease in authorized Full-Time Equivalent (FTEs) state positions of 9,287. This includes a reduction of approximately 2000 positions at state institutions of higher education. The largest FTE reductions are in TDCJ and TYC, nearly 3,400 combined. Nearly every agency has some reduction in FTEs, but it is important to note that the reduction amounts compare budgeted FTEs for FY 2011 with recommended FTEs for 2012 and some percentage of budgeted positions are currently not filled. Since state leaders ordered state agencies to reduce their general revenue appropriations by 5 percent early last year, most agencies have effectively been operating under a hiring freeze.

TPEA is very concerned about the potential for layoffs in the state workforce. The real scale of possible staffing reductions won't become apparent until legislators begin the detailed mark up on individual agencies. TPEA has been working to inform legislators that state agencies have been held to an extremely high standard of efficiency, since they are subject to strict FTE caps and undergo constant scrutiny through the Performance Review and Sunset Review processes. The result is that the size of the state's workforce for general government

(non-higher education) agencies has remained nearly flat for the past decade, growing only 3 percent, as compared with the 28 percent growth in the workforce of state universities, as revealed in a State Auditor's report.

Employee and Retiree Health Benefits



HB 1 appropriates almost \$2.5 billion in funding for the ERS Group Benefits Program, the health care program for active and retired state employees. This is the baseline funding level contained in ERS' Legislative Appropriations Request (LAR), but ERS has estimated this funding level is \$591 million (all funds, \$365 million general revenue) below what is necessary to maintain current benefits. ERS has indicated that this level of funding leaves it with two options. Under one option, state premium contribution levels would have to be reduced from 100 percent for employees and 50 percent for dependent coverage to 80 percent and 40 percent, respectively. A slightly smaller change is also recommended in the LBB Government Effectiveness and Efficiency report. A change to 80/40 contribution levels would shift \$95.53 a month in costs for individual coverage and \$135 a month for full family coverage. Or the other alternative would require the plan to establish large medical services deductibles, between \$2,400 and \$3,400 per participant. Both options shift large costs to employees but would affect participants in different ways.

There are two other LBB Efficiency recommendations regarding health insurance that are added as riders in HB 1. One would require ERS to impose tiered coinsurance so that higher cost plan participants would continue to share in costs above the current \$2000 annual out of pocket coinsurance maximum, although at a lower rate. Currently, participants pay 20 percent coinsurance on expenses up to \$10,000 annually. The proposed new coinsurance tiers would require 5 percent coinsurance above that level, up to \$50,000, and a 2 percent coinsurance above that, up to \$100,000. While this proposal is intended to help reduce medical utilization, it will result in significant additional costs for the relatively small percentage of participants who have high medical costs. The LBB report also recommends tiered coinsurance for higher cost prescription drugs and for changes in cost sharing arrangements for Medicare recipients.

The other LBB recommendation added to HB 1 would impose a \$30 per month tobacco user premium surcharge. This would require tobacco users to pay a \$30 surcharge monthly, both as a disincentive to continuing tobacco use and to help cover the higher average health care costs of smokers and other tobacco users.

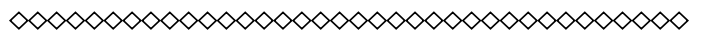
The LBB Efficiency report also recommends changes in premium contributions for retired employees. As with active employees, the report recommends dropping the state share of dependent coverage from 50 to 40 percent for retirees. However, it additionally recommends a tiering of individual retiree premium contributions based on length of service with

the state. This change appears to be retroactive and would affect current retirees, which is extremely problematic.

HB 1 also completely cuts funding for the SKIP program, which is the equivalent of the CHIP program for state employees and helps lower paid employees afford health coverage for their children. TPEA is looking into this issue.

TPEA's legislative goal with regard to health care benefits is to preserve the current premium contribution structure for active and retired employees. The changes proposed by the LBB will simply shift costs and lower take home pay for employees and annuity payments for retirees. Given the scale of the budget shortfall, increasing appropriations for ERS will be difficult, so TPEA is developing other alternative approaches to minimize increased costs to employees and retirees.

ERS Retirement Benefits



HB 1 lowers the state retirement contribution rate from its current 6.95 percent to the constitutional minimum level of 6 percent. Because of changes in state law last session, the recently increased employee contribution rate would also drop to 6 percent. TPEA worked last session to try to help restore the ERS retirement fund to actuarial soundness. A reduction in combined contribution rates will further delay a return to actuarial soundness, which is a necessary condition to allow for any type of benefit increases for ERS retirees.

HB 1 also completely cuts the state contribution to the Law Enforcement and Custodial Officer Supplemental Retirement Fund (LECOSRF).

Finally, the LBB Efficiency report looks at the ERS and TRS pension funds and recommends a study to determine if funding levels or benefits should be changed, or if a hybrid structure should be considered. A rider requiring such a study is included in HB 1. TPEA believes that changes enacted in HB 2559 last session should be given time to take effect and, hopefully, investment returns will improve over the experience of the past decade.

**With Huge Challenges Facing State,
Stay Informed and Involved**



The sheer size of the state's budget shortfall threatens agencies, jobs, and our hard-earned benefits. This could become the most difficult legislative session ever for state employees and retirees. TPEA will continue to do our best to represent your interests and to inform employees and retirees on legislative matters of concern. We also need every state employee and retiree to be informed and involved when needed. If you have not already signed up for TPEA's Advocacy Updates emails, please do so ASAP! Go to www.tpea.org and enter your information into the box in the top left corner of the home page. Encourage fellow employees and retirees to do so also.