



# PUTTING STATE PENSION COSTS IN CONTEXT: TEXAS

<b>2015 Normal Cost of Texas Public Employee Pensions:</b>	<b>\$1,822,777,964</b>
<b>2015 Cost of Texas Subsidies and Corporate Tax Breaks:</b>	<b>\$1,208,518,118</b>
<b>Percentage of Pension Costs to Subsidy Costs:</b>	<b>150.8%</b>

In the 2015 legislative session, the State of Texas and its teachers, corrections officers, and other public employees all agreed to increased contributions to ensure funding stability of the state’s pension systems. A responsible decision by all parties, these measures show the dedication of the state to providing a secure retirement for its public employees. Cities across Texas, like Houston and Dallas, are struggling with similar questions. While this report only focuses on state finances, cities too should ask if their giveaways to corporations are the best way to provide services and a good quality of life to their residents. Dallas politicians, for example, “gave away tens of millions of dollars in property tax abatements, tax increment financing, grants and loans to developers and rich corporations, with an often unmet promise of incredible return on the investment.”<sup>1</sup>

While many pension numbers are circulated in public discussion, the central issue is how much of an obligation is being taken on each year to provide benefits for current government employees such as teachers and first responders. The best way to measure this is to use an amount known as employer normal cost. Such costs can be found in the annual financial reports that each public pension plan has to produce. In the case of Texas the main plans administered by the state are: the Texas Employees’ Retirement System (ERS); the Teachers Retirement System of Texas (TRS); the Law Enforcement and Custodial Officers Fund (LECOF); and the Judicial Retirement Fund, Plan II. The most recent financial reports indicate annual employer normal costs of \$817.1 million for ERS<sup>2</sup>; \$957 million for TRS<sup>3</sup>; \$31 million for LECOF<sup>4</sup>; and \$17.1 million for the Judicial Fund.<sup>5</sup> This equals a total annual normal cost of \$1.82 billion.

How should this amount be viewed? One approach is to compare it to the financial costs incurred by the state in supporting business through economic development subsidies and

other special tax provisions. While not providing an assessment of the effectiveness of any particular subsidy or provision, this approach does provide an important perspective on public sector pensions.

Corporate interests in the state continue to benefit from generous corporate subsidies and other tax breaks. And in February 2017, Gov. Greg Abbott asked the Legislature to increase funding for the state's economic development subsidies by \$200 million.<sup>6</sup>

Two large state authorized property tax programs have slighted local governments of more than \$400 million in property taxes that flowed to private developers rather than public coffers: the state's Chapter 313 reduced local school property taxes paid by businesses by \$221.5 million in 2015 while the Texas Tax Increment Financing (TIF) Act diverted \$186.7 million in property tax revenue from public accounts to benefit private development in TIF Districts.<sup>7</sup> But these local tax diversions also impact the state's budget through provisions in Texas' school funding formula that partially make-up revenues lost to property tax programs. In 2011, make-up payments for TIF cost the state \$171.9 million and in 2015 make-up payments for the smaller tax credit portion of Chapter 313 cost the state \$12 million.<sup>8</sup> No calculations are available detailing costs from the larger property tax abatement portion of Chapter 313.

Other state subsidy programs include: Sales Tax Refunds on Enterprise Projects which deprived the state of \$44.2 million in 2015 and film production subsidies which cost about \$16 million in 2015.

In FY 2015, local economic development corporations spent \$139,100,718 in direct business incentives and \$263,917,400 to retire debt service of projects, all primarily sourced from sales tax revenues.<sup>9</sup> Additionally, no summary of the total costs associated with local Chapter 380 and Chapter 381 grant and loans are available.

Several industries benefit from targeted tax breaks. Internet companies avoid paying sales taxes on servers and other equipment used in data centers; this subsidy cost \$9.2 million. Special tax rates on new or enhanced recovery oil wells cost the state treasury \$41.9 million. Other oil-related tax exemptions cost \$36 million more. The Texas Research and Development tax credit, available across industries, cut state tax revenue by \$3 million in 2015.

Texas also provides generous tax subsidies to oil and gas producers, though it doesn't regularly report on the cost of these subsidies. In 2006, the Texas comptroller studied fossil fuel subsidies and reported an annual cost of \$1.4 billion.<sup>10</sup> Because this data is so old and is likely to be quite different today, we have not included it in our subsidy totals.

A one-year Temporary Permissive Alternative Rates, a large corporate tax break that particularly benefited retailers in the state, cost Texas \$232 million in lost revenue in 2015.<sup>11</sup>

An archaic tax rule that allows retailers to keep a portion of the sales tax revenues they collect from customers (the “vendor discount”) cost about \$251 million in 2015.<sup>12</sup>

Texas is one of the states that allows corporations to apportion their taxable income by methods other than the traditional three-factor (payroll, property and sales) weighting. The Texas tax expenditure report does not contain an estimate of the revenue lost due to its single<sup>13</sup> sales factor apportionment formula, which sharply reduces taxes on firms with substantial capacity and employment in the state, but sell much of their products or services out of state.

The total of these corporate subsidies, official tax breaks and unofficial tax dodging amounts to about \$1.2 billion per year, as summarized in the following table.

State Funds Used to Make Up for Local School Aid Lost to TIF Diversions	\$171,900,000
Temporary Permissive Alternative Rates	\$232,000,000
Sales Tax Vendor Discount	\$251,300,000
Sales Tax Refunds on Enterprise Projects	\$44,200,000
Research & Development Tax Credit	\$43,000,000
Single sales factor	unknown
Special Tax Rate on New or Enhanced Recovery Oil	\$41,900,000
Sales Tax Exemption on Data Center Equipment	\$9,200,000
State Funds used to Make Up for the Tax Credit Losses to Chapter 313	\$12,000,000
Local Economic Development Corps (funded by sales tax)	\$403,018,118
<b>TOTAL</b>	<b>\$1,208,518,118</b>

In other words, the known annual corporate subsidies provided by Texas are sufficient to pay for about 66.3 percent of the taxpayer cost of funding the retirement benefits of current Texas public employees belonging to the main state administered public pensions.

## NOTES

<sup>1</sup>“Don’t let Dallas politicians scare you into taking away firefighter pensions,” by Jim McDade; Dallas Morning News, February 21, 2017. <http://www.dallasnews.com/opinion/commentary/2017/02/21/let-dallas-politicians-scare-taking-away-firefighters-pension>

<sup>2</sup>From 2015 CAFR of Texas Employee Retirement System <http://www.ers.state.tx.us/CAFR2015/> page 106

<sup>3</sup> From 2016 CAFR of Teacher Retirement System of Texas [https://www.trs.texas.gov/TRS%20Documents/cafr\\_2016.pdf](https://www.trs.texas.gov/TRS%20Documents/cafr_2016.pdf) Total normal cost rate of 10.05% less employee contribution rate of 7.7% (page 131) times covered payroll of \$40,742,826,000 (p 90)

<sup>4</sup> From 2015 CAFR of Texas Employee Retirement System <http://www.ers.state.tx.us/CAFR2015/> page 107

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<sup>5</sup> From 2015 CAFR of Texas Employee Retirement System <http://www.ers.state.tx.us/CAFR2015/> page 108

<sup>6</sup> Gov. Abbott seeks more dollars for Taxes' incentive funds (Austin Business Journal) <http://www.bizjournals.com/austin/news/2017/02/02/gov-abbott-seeks-more-dollars-for-texas-incentives.html>

<sup>7</sup> Preceding subsidies mentioned in this paragraph can be found in Tax Expenditures and Tax Incidence Report (Texas Comptroller of Public Accounts, March 2015): <https://www.comptroller.texas.gov/transparency/reports/tax-exemptions-and-incidence/2015/96-463.pdf>

<sup>8</sup> Supplemental school aid figures drawn from "Limit State Funding of School District Participation in Tax Increment Reinvestment Zones (Legislative Budget Board Staff, January 2013) found here: <http://www.txsc.org/wp-content/uploads/2013/01/LBB-Report-on-TIRZ-School-Supplement.pdf>

Chapter 313 tax credit figures drawn from "Additional State Aid for Ad Valorem Tax Credit (Texas Education Agency) found here: [http://tea.texas.gov/Finance\\_and\\_Grants/State\\_Funding/Additional\\_Finance\\_Resources/Additional\\_State\\_Aid\\_for\\_Ad\\_Valorem\\_Tax\\_Credit/](http://tea.texas.gov/Finance_and_Grants/State_Funding/Additional_Finance_Resources/Additional_State_Aid_for_Ad_Valorem_Tax_Credit/)

<sup>9</sup> Tax Expenditures and Tax Incidence Report (Texas Comptroller of Public Accounts, March 2015) <https://www.comptroller.texas.gov/transparency/reports/economic-development-corporation/>

<sup>10</sup> *The Energy Report, 2008*, Texas Comptroller of Public Accounts, Exhibit 28-7, p 372. <http://cpa.texas.gov/specialrpt/energy/pdf/28-GovernmentFinancialSubsidies.pdf>

<sup>11</sup> Subsidies in this paragraph found in Tax Expenditures and Tax Incidence Report (Texas Comptroller of Public Accounts, March 2015): <https://www.comptroller.texas.gov/transparency/reports/tax-exemptions-and-incidence/2015/96-463.pdf>

<sup>12</sup> Tax Expenditures and Tax Incidence Report (Texas Comptroller of Public Accounts, March 2015) <https://www.comptroller.texas.gov/transparency/reports/tax-exemptions-and-incidence/2015/96-463.pdf>

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