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F I S C A L   I M P A C T   R E P O R T

SPONSOR Smith | **ORIGINAL DATE** 02/08/11 | **LAST UPDATED** 02/16/11 | **HB**

SHORT TITLE Reduce PERA Cost-of-Living Adjustments | **SB** 204/aSPAC

ANALYST Aubel

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
		Indeterminate but likely significant reduction*	Indeterminate but likely significant reduction*	Indeterminate but likely significant reduction*	Recurring	General Fund
		$100.0	$50.0	$150.0	Nonrecurring	PERA

(Parenthesis ( ) Indicate Expenditure Decreases)
*See Fiscal Implications

May conflict with HB 58, HB 251, SB 87, SB 88, SB 303
Relates to SB 248 and SB 268

Senate Bill 204 is sponsored by the Investment Oversight Committee.

SOURCES OF INFORMATION
LFC Files

Responses Received From
Public Employees Retirement Association (PERA)
Administrative Office of the District Attorneys (AODA)
New Mexico Corrections Department (NMCD)
New Mexico Municipal League (NMML)

SUMMARY

Synopsis of SPAC Amendment

The Senate Public Affairs Committee amendment clarifies that the cost-of-living adjustment (COLA) shall be “annual and cumulative.” As currently worded, it is ambiguous whether the COLA was applied every year and whether it was applied on the original pension or was cumulative, as specified for the Educational Retirement Board COLA. This amendment helps preserve retirees’ purchasing power over time.

Synopsis of Original Bill

Senate Bill 204 amends the PERA Act to base the cost-of-living adjustment (COLA) on 3/4s the Consumer Price Index (CPI), with a floor of 0 percent and a cap of 3 percent. The current COLA is a flat 3 percent regardless of inflation or age, starting two full calendar years after retirement, and compounds annually. The waiting period is reduced to one full calendar year for disability retirement.

With the effective date of July 1, 2011, the new COLA in SB 204 would apply to all current pension recipients and active members, including those in plans under PERA, the Judicial Retirement Act (JRA), the Magistrate Retirement Act (MRA), and the Legislative plan.

FISCAL IMPLICATIONS

PERA did not provide an actuarial analysis of the bill.

Due to deteriorated funding status, PERA is requesting contribution increases of 2 percent per year for four years (8 percent total) for five plans: State General Plan 3, Municipal Fire, Municipal Police, JRA and MRA. The combined employer contributions associated with the two bills, SB 87 and SB 88, are provided in Table 1.

Table 1 – Combined Fiscal Impact of SB 87 and SB88

	FY12	FY13	FY14	FY15**	4 Year Total Cost	Recurring or Non-Rec	Fund Affected
Employer Contribution Increase – SG3	$11,547.9-$12,478.2	$23,095.9-$24,956.4	$34,643.8-$37,434.6	$46,191.7-$49,912.8	$115,479.3-$124,782.1	Recurring**	Primarily General Fund
Employer Contribution Increase – Muni Police	$3,274.1-$3,421.4	$6,548.1-$6,842.8	$9,822.2-$10,264.2	$13,096.3-$13,685.6	$32,740.7-$34,214.1	Recurring**	Local Gov
Employer Contribution Increase – Muni Fire	$1,674.1-$1,749.4	$3,348.2-$3,498.9	$5,022.3-$5,248.3	$6,696.4-$6,997.8	$6,696.4-$6,997.7	Recurring**	Local Gov
Employer Contribution Increase - JRA	$173.9 - $182.1	$347.8 - $364.3	$521.7 - $546.4	$695.6 - $728.6	$1,738.9 to $1,821.5	Recurring**	General Fund
Employer Contribution Increase - MRA	$46.9 - $49.9	$93.9 – $99.8	$140.8 - $149.6	$187.7 – $199.5	$469.3 - $498.8	Recurring**	General Fund

*Each increment equates to around $11 million general fund for SG3, over $3 million for Municipal Police, $1.7 million for Municipal Fire, and a combined $220 thousand for the judicial plans. The FY15 numbers represent the final recurring employer contribution increase requested by PERA.

Based on a prior analysis performed for the Legislative Finance Committee (see Attachment A), the reduction to the Unfunded Actuarial Accrued Liability (UAAL) by reducing the built-in COLA from an automatic 3 percent to one based on the CPI would most likely be substantial. Reducing the UAAL implies an improvement in PERA's funded status, which would most likely

mitigate or reduce the need for increased contributions to bring the plans into compliance with the industry standards of a thirty-year funding period and an 80 percent funded ratio. Thus, this bill has the potential for a significant savings to the general fund while improving the funding status of PERA. The reduction in the needed contribution rates and associated savings are indeterminate without an actuarial study. Any general fund savings due to the lower employer contribution rate would be recurring.

PERA notes the following administrative impacts and the associated fiscal impacts to the agency's operating budget:

- PERA will incur operating costs related to printing, postage and dissemination of information associated with implementing the reduced COLA benefits. In addition, PERA will require increased staff utilization to review COLA calculations and 1099 reporting will require revisions to PERA's pension administration system ("RIO"). PERA will be required to seek a BAR to cover the costs of these system changes.
- PERA will experience litigation related to SB 204. Lawsuits related to reducing cost-of-living adjustments for existing retirees are currently pending in the States of Colorado, Minnesota and South Dakota. PERA does not have sufficient resources to handle such litigation in house. PERA will be required to seek a BAR to cover the costs of litigation.

PERA estimates these increased operating expenses at $150 thousand; the related costs appear to be non-recurring.

SIGNIFICANT ISSUES

Note: To facilitate discussion, actuarial technical terms are related in more familiar language, such as the Actuarial Value of Assets is simply referred to as "assets" and the Actuarial Value of Liabilities is referenced as "liabilities." The present value of liabilities relies on several actuarial assumptions related to inflation, investment returns and demographics. This discussion assumes all future experience meets these assumptions as well as all assumptions remaining constant.

Senate Bill 204 is an Investment Oversight Committee sponsored bill to improve pension solvency while considering the issue of state solvency.

Defined Benefit Plan

The PERA plans are defined benefit plans, with specified factors that calculate a set pension benefit. For example, for State General Plan 3 members, the pension formula for normal retirement is calculated as follows:

Table 2 - State General Plan 3 Defined Benefit Calculation

Formula: # Years Service credit * Pension Factor *		**Final Ave Salary (FAS) =**	**Pension Benefit**
Example 1:	25 years * 3% = 75% *	$50,000 =	$37,500
Example 2	30 years * 3% = 90% *Benefit is capped by 80% *	$50,000 =	$40,000

*The cap effectively means that no additional benefit is earned after 26.7 years.

In 1992, the PERA COLA was changed to a flat 3 percent compounded annually (See Attachment B.) Based PERA demographics, for a 2009-2010 retiree, the 3 percent COLA would about double the average monthly pension from $2,335 to $4,747 over her expected lifetime.

Pension Solvency
The defined benefit is considered an obligation of the plan sponsor, and actuaries calculate the value of the future benefits based on several assumptions. For long term sustainability of the plan, the funding for all the projected benefits must equal the value of those obligations - or liabilities – according to the following equation:

Pension Sustainability Equation
(I)nvestments + (C)ontributions = (B)enefits + (A)dministrative Expenses

Or
Assets = Liabilities

A general view of plan health can be indicated by how much of the liabilities are covered by assets at any given time. This is called the funded ratio, or

Assets
Liabilities

Due to the market downturn and ensuing negative investment returns for FY08 and FY09 of -7.4 percent and -24.1 percent, respectively, PERA's actuarial value of assets has dropped significantly, lowering the funded ratio for all plans. The losses, which are rolled in over a four year period in a "smoothing" process, are further reduced by not receiving the 8 percent expected return, compounded annually.

Table 3 – Investment Returns "Smoothed" Into PERA Funds

Fiscal Year	Investment Return	Expected 8%	Return "Smoothed" In
FY08	-7.4	Below by 8%	-15.4%
FY09	-24.1	Below by 8%	-32.1%
FY10	15.9%	Above by	7.9%

The June 30, 2010 funded ratio for state General Plan Division was 72.3 percent. A minimum industry standard of the funded ratio is 80 percent. More important is whether this ratio is trending up or down. The trend is downward for this plan as well as for all the plans referenced below.

Table 4 – Trend of Funded Ratio

Plan	Funded Ratio June 30, 2009	Funded Ratio June 30, 2010	Trend
State General Plan 3	77%	72.3%	↓
Municipal Police	86.7%	80.1%	↓
Municipal Fire	74.6%	68%	↓
Judicial	60.5%	61.2%	↓
Magistrate	66.3%	65.8%	↓

The value of the liabilities not covered by the value of assets is called the unfunded actuarial accrued liability, or UAAL. The table below shows the UAAL for each plan as of June 30, 2009 and June 30, 2010. Note that the UAAL is increasing, a sign of plan deterioration.

Table 5 – Unfunded Actuarial Accrued Liabilities (in millions)

Plan	UAAL June 30, 2009	UAAL June 30, 2010	Trend
State General Plan 3	$1,548	$1,934	↑
Municipal Police	$248	$391.5	↑
Municipal Fire	$268	$360.6	↑
Judicial	$47.7	$51.8	↑
Magistrate	$16	$18.0	↑

The amount of time to pay off the UAAL (amortization) is called the funding period. The Government Accounting Stands Board (GASB) has set a minimum standard for amortization of the UAAL of 30 years. The table below shows the funding period as of the last two valuation dates. Note that this measure lies far below the 30-year recommendation: an infinite funding period means that, given all assumptions hold, the UAAL would never be paid off with current contributions as of that date.

Table 6 – Trend of Funding Period

Plan	Funding Period June 30, 2009	Funding Period June 30, 2010
State General Plan 3	111 years	Infinite
Municipal Police	Infinite	Infinite
Municipal Fire	Infinite	Infinite
Judicial	Infinite	Infinite
Magistrate	Infinite	Infinite

The primary issue is that, due mainly to investment returns falling significantly below the plans' 8 percent assumption, the sustainability equation noted above is not in balance and the trends indicate that the plans are moving toward insolvency unless action is taken:

(I)nvestments + (C)ontributions < (B)enefits + (A)dministrative Expenses
Or
Assets < Liabilities

Key Assumption: 8% Investment Return

In fact, the indicators of fund solvency may be optimistic and the difference between the assets and the obligations, or the amount of obligations that are funded, may be greater than what is being reported. A key assumption in valuing the liabilities is the rate at which the future costs are discounted to a present value. Currently, PERA uses an 8 percent investment return assumption. Many plans have lowered that assumption in the expectation of lower expected returns going forward, and others are considering moving to a risk-free rate as low as 4 percent. If a lower discount rate is used to value PERA's obligations, the UAAL would jump dramatically and the corresponding funded ratio and funding period would decline. Table 7 shows PERA's investment return over various periods as of September 30, 2010, which remains below the 8 percent target for the 10-year average of about 4 percent.

Table 7

Fund Performance vs. Relative Benchmarks*

1 Year			5 Year			10 Year		
Fund	Benchmark	Ranking	Fund	Benchmark	Ranking	Fund	Benchmark	Ranking
11.66%	9.39%	27	2.29%	3.88%	96	3.60%	3.26%	69
Median Fund Performance		13.81%	Median Fund Performance		3.15%	Median Fund Performance		3.55%

Core Policy Issue

The central policy issue is what action needs to be taken to ensure public employees receive their pensions and how swiftly the Legislature needs to act. Although the pension boards can make recommendations, unlike some states, New Mexico public pension plans are set in statute and it is the Legislature - with concurrence by the governor - that ultimately makes plan changes.

To address the pension solvency issues recorded by PERA, the Legislature has two options: 1) increase contributions or 2) reduce the value of the pension obligations. Reducing pension obligations entails benefit plan changes; this is called pension reform.

(1) ↑ (2)↓
(I)nvestments + (C)ontributions ↑ < (B)enefits ↓ + (A)dministrative Expenses

The shortfall is determined by the actuarial required contribution (ARC), which calculates the required contribution, based as a percent of payroll, needed to cover the current cost associated with participants and to amortize the UAAL over the GASB 30-year recommendation. The UAAL can go up or down, primarily as a result of investment returns (holding all other factors constant). Thus, the actuaries calculate the ARC on an annual basis. Some public plans must fund any change in the ARC automatically. However, PERA contribution rates are set in statute. For the most part these rates have been sufficient to meet solvency requirements, but the negative FY08 and FY09 investment returns have created significant shortfalls in funding as measured by the ARC less current contribution rates:

Table 8 - Contribution Shortfall

Plan	Contribution Shortfall June 30, 2009	Contribution Shortfall June 30, 2010	Trend
State General Plan 3	4.13%	6.67%	↑
Municipal Police	4.14%	7.49%	↑
Municipal Fire	7.22%	11.04%	↑

Because the actuaries anticipate further declines in PERA's funding measures as additional FY08 and FY09 investment losses are 'smoothed" into their calculations over the next two years, they recommend the enacting the maximum 8 percent contribution rate promulgated by PERA policy.

Note that the Municipal Fire Plan shortfall is over 11 percent; unless investment gains are above the 8 percent assumption or other benefit changes or other experience gains reduce the value of liabilities, it is likely the 8 percent increase will be insufficient to ensure plan sustainability.

Pension Sustainability

Table 9 shows the final contribution rate for State General plan 3 under PERA's scheduled request (SB87) would be 31 percent, with the employer paying 21.92 percent. This is almost a 6 percentage point increase from the current statutory rate (July 1, 2011) of 15.59 percent. The proposed rates for the municipal plans run as high as 45.45 percent for the total contribution, with the employer portion ranging from 26.38 percent to 40.733 percent of salary for each employee depending on the "pick up" rate employed by the governing entity.

Table 9: Proposed Schedule for 8% Pension Contribution Increase - State

	Current Statute	SB87 State General Plan 3				
	FY12	FY12	FY13	FY14	FY15	FY12-FY15 Change
Employer	16.59%	17.92%	19.25%	20.58%	21.92%	5.33%
Employee	7.42%	8.09%	8.76%	9.43%	10.09%	2.67%
Total Contribution	**24.01%**	**26.01%**	**28.01%**	**30.01%**	**32.01%**	
Incremental Increase		2%	2%	2%	2%	8%

Pension sustainability has been defined by Girard Miller, an industry expert, as the ability and willingness of pension sponsors to make contributions into the plans. Due to the recession, the state and municipal plan sponsors have seen a reduction in revenues to support contributions. State solvency measures in 2009 and 2010 partially depended on reducing the burden for state employers by shifting 1.5 percent of the employer contributions to the employee and delaying the ERB 0.75 percent employer increase by one year.

Given the projected budget deficit of at least $215 million for FY12 and reduced revenue projections for the foreseeable future as the economy recovers, it is questionable whether the sponsors have both the "ability and willingness" to support the plan benefits as currently structured in a sustainable manner.

These benefits are among the most generous for public employees in the nation, especially after the rush of pension legislation over the last two years as plan sponsors scrambled to address pension solvency issues due to the 2008-2009 market meltdown in the face of economic woes.

Pension Reform

According to the National Conference of State Legislators, 20 states have implemented higher contribution rates and/or pension reform in 2010 to address pension solvency issues. Due to concerns regarding property and contractual rights, much of pension reform focuses on new hires. Such pension reform takes years to impact solvency and does little to address current pension liabilities.

Some states have taken more aggressive action to strengthen funds by aligning pension structures with new demographic and economic realities. South Dakota, Colorado and Wisconsin enacted legislation that impacted current employees and also retirees—such as reducing the cost of living adjustment (COLA). Lawsuits filed in these states are being closely watched for how courts will view pension rights.

Table 10 - Selected COLA Changes – 2010

	From	To	Members
Colorado PERA	3.5% per year	Lesser of 2.0% CPI of negative return in last 3 years, with funded ratio rules	All members
Illinois	3.0% per year	Lesser of 3.0% per year or 50% of CPI	New members on or after January 1, 2011
South Dakota RS	3.1% per year	3.1% if funded ratio (FR)>90%, 2.6% if 90%, 2.6% if FR between 80%-90%,2.1% if FR<60%	All members

Source: Buck Consultants

The New Mexico Constitution (Article XX, Section 22) states that vested employees acquire a property right to pensions. However, Article XX, Section 22 (E) states that "Nothing in this section shall be construed to prohibit modifications to retirement plans that either enhance or preserve the actuarial soundness of an affected trust fund or individual retirement plan."

Laws 2009, Chapter 288, established 30-year eligibility for new hires for the education retirement system and PERA non-public safety plans. This established what is termed a "second tier" to the plans. The legislation also set up a 25-member task force to study the plans and make recommendations for the 2011 legislative session to address pension solvency. The task force made few final recommendations. Any challenges to pension reform applied in New Mexico will ultimately need to be resolved by the courts.

PERFORMANCE IMPLICATIONS

The COLA is the most expensive part of the PERA benefit. PERA testimony has ranged from 25 percent to 30 percent of the cost of the defined benefit plan. Reducing the COLA, or at least basing it on some measure of plan funding, would improve the solvency indicators for PERA. Most importantly, it would reduce the UAAL and improve the funded ratio as well as the funding period.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Senate Bill 204 may conflict with the bills calling for contribution increases (HB 58, SB 87 and SB 88) because a reduction in the COLA may mitigate or eliminate the need to increase contributions.

Senate Bill 204 may also conflict with HB 51, which also proposes reduced COLA and increased age and service requirements for ERB and PERA.

Senate Bill relates to SB 248, which reduces the employer's burden for pension contributions due to state solvency concerns.

SB 204 relates to PERA's "ideal" plan that uses the same COLA formula as part of its new proposed plan packages for new hires that reduce both plan benefits and plan costs.

OTHER SUBSTANTIVE ISSUES

PERA provides a history of the COLA in a February 4, 2004 memo (See Attachment B):

> Until 1992, the PERA Act's cost-of-living provisions contained an "adjustment factor," which reflected the change in the consumer price index (CPI), with a minimum and maximum range for any year. Calculation of the adjustment factor varied from year to year, but typically was determined by dividing the CPI for the preceding year by the CPI for the next preceding calendar year, with the result being rounded to three decimals. In 1992, the PERA Act was amended to remove all reference to the CPI and provided for a fixed-rate COLA at 3%.

In this memo, PERA provided a comparison of the impact of changing from a CPI-based COLA to the 3 percent COLA, indicating that at the end of the 10-year period from 1994 to 2004, "the

annual 3 percent COLA gives the member a monthly benefit that is 6.2% higher than if the COLA was based directly off the CUI-U" (CPI-Urban).

Current benefits allow most current employees to work for 25 years and retire, which no longer aligns with demographics where people are living longer and drawing a pension longer. Table 11 provides a snapshot of PERA members as of June 30, 2010.

Table 11 -PERA MEMBERSHIP DATA – STATE GENERAL PLAN
(Dollars in millions)

STATE GENERAL PLAN	2000	2010	Change
Active Members	20,108	20,867	3.6%
Retired Members	8,089	12,981	37.7%
Ratio of Active/Retired	2.5/1	1.6/1	Ratio is declining
Employer Payroll	$607.4	$866.1	29.9%
Retiree Payroll	$133.1	$313.4	57.5%
Total Contributions	$143	$248.4	42.4%
Average age at retirement State General* State Police/Corrections		 57.91* 48.67	
Longevity Expectations* Men Women		At average retirement* 81.32 84.78	

Senate Bill 204 is based on the idea of "shared sacrifice" of all the various member groups: retirees, vested and unvested active members, and new hires rather than placing the entire burden on contribution increases and new hires.

ALTERNATIVES

One alternative that would ensure the legislative intent to address pension solvency was clearly articulated would be to tie the COLA change to a solvency metric and/or investment returns, such as those put in place in Table 10 for Colorado and South Dakota.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

The pension plans will continue to show a deteriorated funding status absent other actions to reduce the liabilities or increase contributions, holding all other factors constant.

MA/mew:bym:svb

NEW MEXICO PUBLIC EMPLOYEES' RETIREMENT ASSOCIATION
SUPPLEMENTAL VALUATION REPORT AS OF JUNE 30, 2009
COST-OF-LIVING ADJUSTMENT ACTUARIAL STUDY

Actuarial Statement

The estimated impact on PERA system costs for the **State General** Division is illustrated below:

	UAAL ($Mill)	UAAL %	Normal Cost %	Total Contribution %	Statutory Rate	Short Fall
Total Prior to Proposal (Based on 30 yr amort)	$ 1,547.7	8.49%	19.65%	28.14%	24.01%	4.13%
Increase/(Decrease) For						
Current Retirees	$ (552.6)	(3.03)%	0.00%	(3.03)%		
Current Actives with 5 or More Years of Service	$ (335.6)	(1.84)%	(1.32)%	(3.16)%		
Current Actives with Less Than 5 Years of Service	$ (20.2)	(0.11)%	(0.62)%	(0.73)%		
Total Increase/(Decrease)	$ (908.4)	(4.98)%	(1.94)%	(6.92)%		
Total After Proposal (based on 30 yr amort)	$ 639.3	3.51%	17.71%	21.22%	24.01%	none

Comments:

1. If the proposal applied only to new hires, then the normal cost would decrease gradually over the next 20 years. The ultimate reduction in normal cost (once all the current active members have been replaced) would be approximately 1.65% of payroll (there would be no change in the unfunded accrued liability as a result of changing benefits for new hires only).
2. Percents shown are percent of payroll for the division of $935,865,642.
3. If the change had been made to the plan as of June 30, 2009 and applied to ALL members, the amortization period as of June 30, 2009 would have been 22 years, presuming no change in the statutory contribution rate.
4. UAAL = Unfunded Actuarial Accrued Liability.
5. The shortfall is the amount of additional contributions necessary to meet the Board funding objective of 30-year financing. "None" means that the current statutory contributions result in a financing period less than or equal to 30 years.

Attachment A

PUBLIC EMPLOYEES RETIREMENT ASSOCIATION OF NEW MEXICO
PUBLIC EMPLOYEES RETIREMENT BOARD
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JEFF A. VARELA, Chairman
State Member

TERRY SLATTERY, CEBS
Executive Director

MEMORANDUM

TO: **LEGISLATIVE COMMITTEE**

FROM: **Susan G. Pittard, General Counsel**
Chris Bulman, Assistant General Counsel

RE: **PERA Historical Cost-of Living Adjustment ("COLA") Statutes**

Date: **February 4, 2004**

At the January 6, 2004 Legislative Committee meeting, staff was directed to provide a historical summary of the PERA Act's cost-of-living statutory provisions and their funding sources. In addition, staff was asked to discuss what effect the constitutional amendment codified at Article 22, Section XX of the New Mexico Constitution would have on future modifications to the PERA Act's COLA provision.

Until 1992, the PERA Act's cost-of-living provisions contained an "adjustment factor," which reflected the change in the consumer price index ("CPI"), with a minimum and maximum range for any year. Calculation of the adjustment factor varied from year to year, but typically was determined by dividing the CPI for the preceding year by the CPI for the next preceding calendar year, with the result being rounded to three decimals. In 1992, the PERA Act was amended to remove all reference to the CPI and provided for a fixed-rate COLA calculated at 3%. Attached at Exhibit 12 is a table comparing the effect of the CPI-U for the past 10 years to PERA's current 3% COLA.

The following timeline provides the statutory authority for COLAs since their inception under the PERA Act:

1965 through 1971

Effective July 1, 1965, PERA's first "Annual Increase in Annuity" at a fixed rate of 2% per year on the base annuity with no minimum or maximum adjustments.

965 N.M. Laws, ch. 284, § 9. [Exhibit 1].

1971 through 1973

Effective July 1, 1971, statute was renamed "Cost of Living Adjustment." COLA increased to 2.3%, less any amounts received in prior years of 2% adjustments.

- *Retirees opting to receive the increased benefit were required to make a one-time lump-sum payment of 1% of final average salary for the increased COLA benefit.*

1971 N.M. Laws, ch. 292, § 3. [Exhibit 2].

Effective July 1, 1973 and continuing through June 30, 1978, the Legislature approved varying COLA rates as follows:

1973 through 1975

- Authorized COLAs of between 0.25% and 6.00%, based upon a member's date of retirement, effective July 1, 1973. All persons retired prior to July 1971 received the full 6% adjustment.
- In cases where application of the percentage adjustment resulted in less than $5 per month, the statute mandated a minimum $5 increase.
- *The cost of these increases were funded from mortality saving and excess earnings of the Retirement Reserve Fund.*

1973 N.M. Laws, ch. 334, § 1. [Exhibit 3].

1975 through 1978

- Authorized COLAs of 6.00% for all annuities, effective July 1, 1975. Increased minimum adjustment to $10 per month and imposed a maximum adjustment of $25.00 per month.

1975 N.M. Laws, ch. 151, § 1. [Exhibit 4].

1978 through 1979

The Legislature authorized COLAs ranging from 3 to 10 % funded for one year only as follows:

- 10% increase for members who retired prior to July 1, 1975, with the minimum adjustment set at $15 per month, and the maximum adjustment capped at $25.00 per month.
- 6% increase for members who retired between July 1, 1975 and July 1, 1976, with a minimum adjustment of $10 per month and a maximum adjustment of $25.00 per month.
- 3% increase for members who retired between July 2, 1976 and July 1, 1977, with a minimum adjustment of $10 per month and a maximum adjustment of $25.00 per month.

❖ *The cost for this COLA was through a one-time appropriation of $718,000 from the State General Fund.*

❖ *The PERA Board was specifically authorized by the Legislature to assume the above COLAs beyond June 30, 1979 for the life of the affected retirees at an actuarial cost of $13,500,000.*

1978 N.M. Laws, Special Session, ch. 4, § 5. [Exhibit 5].

1979 through 1982

Effective July 1, 1979, the PERA Act was amended to include a permanent COLA tied to the consumer price index, with the maximum adjustment limited to 2% per year. Adjustments were deferred for new retirees for a period of 5 calendar years.

❖ *The cost of the increased COLA was funded by an increase in contributions as percentages of payroll as follows*:

State General:	1.30%	(employee 1.15% employer .15%)
Municipal General:	.80%	(employee .40% employer .40%)
State Police:	1%	(employee 1%)

1979 N.M. Laws, ch. 333, § 1. [Exhibit 6].

1981 ad hoc CoLA

- Granted an ad-hoc CoLA of $1.00 per month for every year of service credit and $1.00 per month for every year retired, applicable to all members who were retired as of July 1, 1980, effective July 1, 1981. The cost of this ad hoc COLA was $10,000,000.

  - *In 1981 it was the policy of the PERA Board to recommend to the legislature that contingencies from mortality savings or excess earnings be paid to retirees in the form of an ad hoc COLA.*

1981 N.M. Laws, ch. 139, § 1. [Exhibit 7].

1982

The PERA Act was amended to permit COLA increases of 3% per year, and reduced deferral period to 2 calendar years following retirement.

- *The cost of the increased COLA was funded by an increase in contributions as percentages of payroll as follows:*

State General:	1% (employee .50% employer .50%)
Municipal General:	1% (employee .50% employer .50%)

- *A transfer from the Employer Contribution Fund in the amount of $20,000,000 to the Retirement Reserve Fund to cover the 5,000 retirees on payroll.*

1981 N.M. Laws, ch. 228, §§ 2, 5. [Exhibit 8].

1985 amendment

Effective July 1, 1985, the PERA Act was amended to further reduce the COLA deferral period to 1 calendar year following retirement for disability retirees and those retirees who were 65 years or older, effective July 1, 1985.

- *The actuarial cost projected was .6% of active member payroll or approximately $3 million dollars per year, or to extend the amortization period 10 years, which was the final decision of the PERA Board.*

1985 N.M. Laws, ch. 162, § 1. [Exhibit 9].

1987 amendment

Clarified that consumer price index figure ("CPI") should be based upon Department of Labor numbers for "urban consumers." Also authorized the PERA Board to select an "alternative index" if the CPI was discontinued or substantially restructured.

Specified a 2-year COLA deferral period for survivor beneficiaries.

1987 N.M. Laws, ch. 253, § 118. [Exhibit 10].

1992 through present

Effective July 1, 1992, the PERA Act was amended to remove all references to the consumer price index and provided a fixed annual COLA of 3%.

- *This increase to a permanent fixed-rate COLA reflected the maximum range of the adjustment factor previously used by PERA's actuaries to determine the annual COLA rate annually. As a result, no funding source was identified for this increase.*

1992 N.M. Laws, ch. 116, § 8. [Exhibit 11].

1998 Article XX, Section 22 Constitution of the State of New Mexico

Effective November 30, 1998, the New Mexico Constitution was amended, in pertinent part, to state:

> The legislature shall not enact any law that increases the benefits paid by the system in any manner or changes the funding formula for a retirement plan unless adequate funding is provided.

The constitutional amendment precludes the legislature from creating additional liabilities to the retirement system without providing adequate funding for those liabilities. An amendment to the PERA Act that increases the benefits paid by PERA without adequate funding on an actuarial basis is contrary to Article XX, Section 22 of the New Mexico Constitution. All adjustments to the PERA Act's COLA statute, including COLA rate increases, reduction of deferral periods or ad hoc COLAs, become permanent liabilities to the retirement system and require a funding source for them to be deemed constitutional.

cc: Terry Slattery
Mary Frederick
Kurt Weber

COMPARISON OF EFFECT OF CPI-U TO ANNUAL 3% COLA FOR PERIOD 1994 THROUGH 2004

DATE	CPI-U	AMOUNT	3% COLA	AMOUNT
12/94		$1,000		$1,000
7/95	2.7%	1,027	3%	1,030
7/96	2.5%	1,053	3%	1,061
7/97	3.3%	1,088	3%	1,093
7/98	1.7%	1,107	3%	1,126
7/99	1.6%	1,125	3%	1,160
7/00	2.7%	1,155	3%	1,195
7/01	3.4%	1,194	3%	1,231
7/02	1.6%	1,213	3%	1,268
7/03	2.4%	1,242	3%	1,306
7/04	1.9%	1,266	3%	1,345

At the end of this 10-year period, the annual 3% COLA gives the member a monthly benefit that is 6.25% higher than if the COLA was based directly off the CPI-U.

EXHIBIT
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