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

SPONSOR Nava **ORIGINAL DATE** 02/17/11 **LAST UPDATED** **HB**

SHORT TITLE Identical Benefits for Some Public Employees **SB** 303

ANALYST Aubel

REVENUE (million)*

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY11	FY12	FY13		
0.75% Employer increase (Compared to FY11)	$20.1 million	$40.2 million	Recurring	ERB

(Parenthesis ( ) Indicate Revenue Decreases)
*See fiscal impact.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
State General Plan 3 – compared to FY11*		$12,991.4	$12,991.4	$25,982.8	Recurring	State Agencies - all funding sources
Education Retirement-compared to FY11*		$57.8 million	$77.9 million	$135.7 million	Recurring	All funding sources- ERB employers
Actuarial Report		$25.0-$50.0			Nonrecurring	PERA

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

Conflicts with SB 87, SB 204, SB248, SB 265 and HB 133
Relates to SB 88
Relates to Appropriation in the General Appropriation Act

SOURCES OF INFORMATION
LFC Files

Responses Received From
Educational Retirement Board (ERB)
Public Employees Retirement Association (PERA)

New Mexico Public Education Department (PED)
Administrative Office of the District Attorneys (AODA)
New Mexico Corrections Department (NMCD)
New Mexico Department of Transportation (NMDOT)

SUMMARY

Synopsis of Bill

PERA summarizes the bill's provisions:

Amends the Public Employees Retirement Act and Educational Retirement Act to provide identical retirement eligibility requirements, contribution rates, final-average-salary calculations, and cost-of-living adjustments for new members on or after January 1, 2014, as follows:

- Increases the PERA Act's state member employee contribution rate of 7.42% to 7.66% and reduces the employer contribution rate of 16.59% to 15.245%.

- Increases the PERA Act's method of calculating final average salary for all members to one forty-eighth of the greatest amount of salary paid a member for 48 consecutive months of service (from 36);

- Increases the Educational Retirement Act's cost-of-living adjustment (COLA) to 3% annually to be identical with PERA's COLA.

SB 303 requires the PERA Board and the ERB to conduct actuarial studies to determine the amount of pension to be paid to general members first employed on or after January 1, 2014, using SB 303's amendments to the respective retirement systems. Studies are to be reported to the legislature on or before December 1, 2012.

FISCAL IMPLICATIONS

The bill changes the contributions for the new plans with the following fiscal impacts.

FY12 Impact from Allowing the 1.5% Contribution Shift Sunset and 0.75% ERB Increase
The employer and employee contributions rates will remain as stipulated in current statute for employees that are members prior to the effective date of December 31, 2013. Because the bill does not impact the contribution rates or the pension benefits for these employees, there is no fiscal impact when compared to statute.

However, when comparing the budget needs for FY12 under the bill to those funded for FY11, the bill would require additional funding for state employers to pick up the 1.5 percent contribution shift that is not included in either the LFC or the executive budget recommendations. Using the June 30, 2010 reported valuation annual payroll of $866.1 million for State General Plan 3, the estimated additional funds needed equal about $13 million. The general fund component is unknown but, presumably, would account for most of this fiscal impact.

The bill preserves the 0.75 employer contribution increase set for FY12 as well as the sunset of the 1.5 percent shift, which when combined, produce at the employer contribution rate of 13.15 percent. This rate represents a 2.25 percent increase from FY11. As with the State General Plan 3, the LFC and executive budget recommendations do not fund this additional 2.25 percent for FY12. Based on the FY10 actuarial salary reported for ERB of $2.5 billion for those making $20,000 or less, the 1.5 percent shift, including all funds, the recurring fiscal impact to educational employers beginning FY12 would be about $57.8 million, with $37.7 million due to the 1.5 percent shift and $20.1 million due to the 0.75 percent. The $20 million associated with the 0.75 would represent a new revenue stream to ERB, representing both revenue to ERB and operating expenses to ERB affiliates for K-12 and higher education. If funded, the recurring general fund impact would be about 89 percent.

The bill also preserves the subsequent 0.75 percent employer increase set for FY 13 to bring the final employer rate for pre-2014 employees to 13.9 percent. This fiscal impact, again, yields another $20.1 million as revenue and recurring expenses to ERB employers.

For new employees starting January 1, 2014, the contribution rates change, as follows:

As of January 1, 2014	Employee	Employer
Current Statute: State General Plan 3	7.42%	16.59%
SB303- SGP3	7.66%	15.245%
Change	+0.24%	-1.345%
Net Change	-1.105%	

This net change, beginning January 1, 2014, will reduce revenue going to the PERA State General Plan 3 by 1.1 percent. PERA did not provide an actuarial analysis of this change but it would only take effect over time as the new employees were hired. The revenue decline and actuarial impact are indeterminate without the analysis and would be based on the expected rate of retirement of pre-2014 employees and the hiring of post-2014 employees.

As of January 1, 2014	Employee	Employer
Current Statute: ERB	7.9%	13.9%
SB303- ERB	7.66%	15.245%
Change	-0.24%	+1.345%
Net Change	+1.105%	

Thus, SB 303 effectively transfers 1.1 percent of the total contributions going into the pension plans from PERA's State General Plan 3 to ERB. According to ERB, the contribution transfer is not sufficient to bring the fund into an 80 percent funded ratio within 30 years but does improve the funding period from infinite to 14.7 years by 2040, all assumptions holding constant. The bill enhances the COLA for ERB post-2014 employees, which works against the increased contributions.

ERB's concerns regarding the fiscal implications focus on the proposed enhanced cost-of-living adjustments (COLA) for ERB members. Currently, the ERB COLA starts after age 65, not two calendar years after retirement. In addition, it is based on inflation, not a set 3 percent compounded per year. Based on the PERA COLA, which has been described as contributing up to 30 percent of the cost of the plan, the actuarial impact could be significantly negative for the ERB fund. It is likely that other benefits would need to be reduced in the final plan design to compensate for this COLA.

Operating Impacts

PERA is concerned that SB 303 does not contain appropriations to fund the actuarial studies that it requires PERA and ERB to conduct. The actuarial benefit adequacy study undertaken by the PERA Board in 2009-2010 cost $220,000, although smaller benefit studies for individual plans have ranged from $25,000 to $50,000.

Thus, PERA proposes that SB 303 will have a negative fiscal impact on PERA's operating budget. The agency is clear on its position regarding legislative requests for actuarial studies:

> PERA's professional services agreement with its actuaries covers an annual valuation and experience studies for each of its 5 retirement funds. PERA's existing operating budget does not include funds for the actuarial study request proposed under SB 303. It is not appropriate that Trust Fund monies be used to pay for actuarial studies requested by the legislature. Such requests will need to be paid for by the Legislative Council Service… It would be inappropriate to use trust fund monies to provide actuarial information for a specific group if the benefit of the study did not accrue to all members, retirees and beneficiaries

However, in prior years, PERA included a margin in the professional services contract for up to seven actuarial studies to be performed as requested during the legislative session. It is unclear why this practice has not been extended under the new actuarial contract.

SIGNIFICANT ISSUES

The apparent disparity between the benefits for members retiring under the State General Plan 3 and those provided under ERB has been a matter of much debate over the years. Whether the original premise that ERB employees worked less than a full year, having summers off, is still relevant adds to that debate. Furthermore, a new issue arises regarding the disparity in the contribution rate and COLA for members pre- and post-January 1, 2014. Finally, new disparities arise among the various PERA plans remaining unaffected by the bill. For example, all the uniform members and judicial or magistrate plans would keep the final average salary computations currently in statute.

PERA provides the following background information on the proposed actuarial study:

> <u>Actuarial Study</u>
> PERA has already performed the actuarial study proposed under SB 303. Beginning in 2009, the PERA Board and its actuaries performed a Benefit Adequacy Study that selected between 10 and 20 similar retirement systems based on state population, regional location, size of plan membership, plan coverage (uniformed and non-uniform, social security covered and non-covered) and benefit complexity. The PERA Board looked at a benefit comparison of PERA retirement benefits and the 5 most comparables plans, component by component, such as benefit eligibility, benefit multiplier, FAS period, member contributions, optional forms of payment, and types of purchasable service.

The PERA Board used this Benefit Adequacy Study in conjunction with the Legislature's concerns regarding the sustainability of the retirement system to direct their actuaries to create an "ideal" proposed plan for new hires after a certain date. Senate Bill 268 creates the PERA Board's proposed "ideal" plan with contribution rates determined to cover the long-term cost of the proposed plan based on the data and assumptions used for PERA's June 30, 2009 annual actuarial valuation:

- The Normal Cost for the proposed plans is *lower* because the benefits provided are reduced;
- Statutory contribution rates are based on more conservative assumptions to reduce the chances that rates will need to be adjusted as a result of adverse fund experience.

Currently, a PERA employee's final average salary is based on the highest salary the employee received for any consecutive 36-month period. SB 303 proposes this be extended to a consecutive 48-month period, reducing the PERA benefit. ERB has a five-year FAs computation, which would be enhanced under the bill using a four-year period.

PERA wonders if providing identical retirement eligibility requirements without first determining the respective actuarial impact to the respective retirement systems would be actuarially sound. A secondary issue is whether setting in motion certain contributions benefits and rates before having a complete idea of what the final benefit package would need to be to ensure actuarial soundness of funds is prudent.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

<u>Conflicts with</u>:
SB 87 amends the Public Employees Retirement Act to increase the statutory contribution rates for certain member coverage plans.

SB 204, reducing the cost-of-living adjustment (COLA) effective July 1, 2011 for all current retirees and active members of PERA, JRA and MRA.

SB248, swapping an additional 1.75% of the state's employer contribution rate to employees for a two-year period.

SB 265, establishing a second tier of reduced retirement benefits for both general and public safety members on or after July 1, 2012.

HB 133, delaying the ERB employer contribution increases.

HB 251, establishing a minimum retirement age of 55 years and a reduced COLA for PERA members who are first eligible to retire on or after July 1, 2014.

<u>Relates to:</u>
SB 88 amends the Judicial Retirement Act and Magistrate Retirement Act to increase statutory contribution rates.

ALTERNATIVES

PERA suggest to "adopt SB 268, PERA's 'ideal plan' that was developed by PERA's actuaries after a benefit adequacy study was performed."

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Contributions will remain as specified in statute or altered under other legislation enacted. ERB members and non-uniformed members of PERA hired after July 1, 2010 have 30-year retirement eligibility with no changes to benefit structure.

MA/svb