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

SPONSOR Beffort **ORIGINAL DATE** 01/31/12 **LAST UPDATED** **HB**

SHORT TITLE Public Employee Salary Tiers & Retirement SB 115

ANALYST Smith

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY13	**FY14**	**FY15**		
	Negative		Recurring	PERA & ERB

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION
LFC Files

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

SUMMARY

Synopsis of Bill

Senate Bill 115 temporarily changes the employer and employee contribution rates based on salary tiers for the Judicial Retirement Act, the Magistrate Retirement Act, the Educational Retirement Act, and the following coverage plans administered by PERA: State General Member Plan 3 (applicable to most state employees), State Police and Adult Correctional Member Plan 1, and State Hazardous Duty Member Plan 2.

The new contribution rates for the period July 1, 2012 to June 30, 2013 (FY13) require public employees earning over $50,000 per annum to contribute an additional 1.75% of salary to the retirement funds and applies corresponding reductions in employer contribution rates.

For the period July 1, 2013 to June 30, 2014 (FY14), the revised rates requires public employees earning over $100,000 per annum to contribute an additional 1.5% of salary to the retirement funds and applies corresponding reductions in employer contribution rates.

Currently, state employees are under the effect of 2 separate contribution swaps: 1) a swap of 1.5% from employer to employee through FY13; and 2) an additional swap of 1.75% from employer to employee through FY12. This second swap is targeted to sunset June 30, 2012 given targeted economic measures being met.

FISCAL IMPLICATIONS

Any reduction in employer contributions will negatively impact the PERAs and ERBs actuarial solvency. Employee and employer contribution rates are statutory by member coverage plan. Rates of separation from active membership are used to measure the probabilities of active members terminating that status and requesting a refund of their employee contributions. Rates of withdrawals of active members differ among the demographics of the employee groups. Conversely, employer contributions are nonrefundable and remain in the respective retirement funds. If the total contributions are kept the same, but some of the contributions are shifted from employer to employee, the amortization period for that plan will increase. For the most part, the increase should be small. However, the more poorly funded a group is, such as ERB and PERA's Judicial Fund, the bigger the impact will be. In addition, the closer the normal cost is to the total contributions coming in, the greater the impact will be, such as in the PERA's Magistrate Fund.

SIGNIFICANT ISSUES

- Despite the ERB's poor one-year rank, it still remains the only New Mexico fund to rank higher than the 25th percentile for the past five years; all other funds ranked well in the last quartile of their peer groups for the five-year period.

Three-Year Trend of Funded Ratios FY09-FY11

Fund	June 30, 2009	June 30, 2010	June 30, 2011
ERB	67.5%	65.7%	61.6%
PERA	84.0%	78.5%	70.5%

Source: Pension Valuations

- Realizing returns less than the assumed long-term rate adds to the plans' unfunded liabilities. In April, 2011, the ERB decreased the investment return assumption to 7.75 percent, down from 8 percent. As a result the unfunded accrued actuarial liabilities (UAAL) increased by $473 million, bringing the total UAAL for 2011 to $5.9 billion. Additionally, the PERA also decreased its assumed returns from 8 percent to 7.75 percent. The PERA had a substantial increase in its unfunded liability to nearly $5 billion

- Despite large investment gains for FY10 and FY11, both plans show weaker funded ratios – indicators of plan solvency that compare plan assets to pension obligations. Having 80 percent of obligations covered by assets (funded ratio) has traditionally been viewed as a minimum industry indicator of fund health. Neither plan meets that basic metric nor are they improving. Both plans go far beyond the recommended period of time to pay off the UAAL of 30 years established by the Governmental Accounting Standards Board. Both the ERB and PERA sit on an aggregate period that is now infinite, meaning – given all assumptions holding true – the debt would never be paid off for all its plans.

- New Mexico offers a defined pension benefit plan, calculating benefits based on years of service and highest average salary. The benefits include cost-of-living adjustments (COLAs) that accrue automatically and are tied to the Consumer Price Index (CPI) for inflation. In light of the recent recession and continued growth of pension liabilities, many state legislatures are considering modifying contractually vested rights in the name of state solvency. As a sovereign power, a state has the right to adjust any long-term contract that is largely unfair to one party (taxpayers).

- The Legislative Council Service hired Buck Consultants in 2010 as an independent actuarial firm to advise the task force. While the firm offered valuable recommendations for improving actuarial methods and assumptions for the PERA and the ERB, the firm found the ERB will become insolvent by 2039 and the PERA by 2058, because assets are not growing as fast as the benefits paid out.

ADMINISTRATIVE IMPLICATIONS

SB 115 will have a negative impact on PERA's and ERB's operating budget. Creating a system of tiered contribution rates after July 1, 2012 will require system changes to PERA's RIO integrated pension administration system.

SS/svb