Minutes
of the
First Meeting
of the
Retirement Systems Solvency Task Force
June 10, 2009

The first meeting of the retirement systems solvency task force was called to order at 1:10 p.m. on June 10, 2009 in Room 322, State Capitol, by Raúl Burciaga, lead staff, in the absence of an elected chairperson.

Present
Rep. Mimi Stewart, Co-Chair
Tito Chavez, Co-Chair
Oscar Arevalo
Rep. Richard J. Berry
Charles Bowyer
Sen. Pete Campos
Bill Fulginiti
Rep. John A. Heaton
Emily Kane
Michelle Lewis
Alexis Lotero
Christine Trujillo
Jeff Varela
Rep. Luciano "Lucky" Varela

Absent
Jan Goodwin
Sen. Phil A. Griego
David Heshley
Bruce Malott
Dr. Moshe Arye Milevsky
Sen. Steven P. Neville
Andrew Padilla
Wayne Propst
Terry Slattery
Sen. John Arthur Smith

Staff
Raúl Burciaga and Jonelle Maison, Legislative Council Service (LCS)
Michelle Aubel and David Archuleta, Legislative Finance Committee (LFC)
Bill Walsh and Mark Tyndall, Retiree Health Care Authority (RHCA)
Chris Schatzman, Educational Retirement Board (ERB)
Mary Frederick and Susan Pittard, Public Employees Retirement Association (PERA)

Guests
The guest list is in the meeting file.

Copies of all presentations are in the meeting file.

Paula Tackett, director of the LCS, explained the New Mexico legislative council's policies regarding the establishment of a quorum and the rules of voting. Member designees may be counted to establish a quorum, but designees may not vote. Once established, a quorum is presumed to be present for all actions of the body, unless the presence of a quorum is challenged. Ms. Tackett pointed out that while the law creating the task force provided that members "shall receive per diem and mileage", the bill did not carry an appropriation.

Nonlegislative members may need to look to their organizations for reimbursement for per diem and mileage.

Officers

On motion of Mr. Fulginiti, seconded by Senator Campos, Representative Stewart and Mr. Chavez were elected as co-chairs of the task force.

Primer on Retirement and Retiree Health Care Systems — Systems Representatives

PERA — Ms. Frederick, deputy executive director; and Ms. Pittard, general counsel (written testimony)

The PERA system has 60,077 active members in 31 different retirement plans through 331 participating employers and 435 volunteer fire departments. It also has 25,506 retirees and beneficiaries. Employee contributions range from 4.78 percent to 16.65 percent; employer contributions range from seven percent to 25.72 percent. Of the 31 plans administered, eight are closed to new members. The remaining 23 plans and the number of years a member needs to retire at any age are:

25-year retirement plans:
state general member coverage plan 3
state hazardous duty member coverage plan 2
municipal general member coverage plan 1
municipal general member coverage plan 2
municipal general member coverage plan 3
municipal general member coverage plan 4
municipal police member coverage plan 1
municipal police member coverage plan 2
municipal fire member coverage plan 1
municipal fire member coverage plan 2

25-year retirement plans with a 20 percent service credit enhancement (provides retirement with 20 years and 10 months of service credit):
state police and adult correctional officer coverage plan 1
municipal detention officer member coverage plan 1

20-year retirement plans:
municipal police member coverage plan 3
municipal police member coverage plan 4
municipal police member coverage plan 5
municipal fire member coverage plan 3
municipal fire member coverage plan 4
municipal fire member coverage plan 5

Other active plans with various retirement requirements:

magistrate retirement plan 1
judicial retirement plan 1
state legislator member coverage plan 1
state legislator member coverage plan 2
volunteer firefighter retirement plan

Service credit purchases

After vesting with five years of earned service credit, PERA members are eligible to purchase the following service credits:

non-intervening military service — up to five years
additional service credit (air time) — up to one year
civilian prisoner of war — up to five years
cooperative work study programs — up to five years
employed by a utility company, library, museum, transit company or nonprofit organization taken over by a PERA-affiliated public employer — up to five years.

Members may reinstate forfeited service credit (service credit that was refunded previously) at any time after being reemployed by a PERA affiliate. Ms. Frederick noted that air time is the most expensive service credit purchase option because the price is determined by the actuarial cost. For all service credit purchases, the employee is required to pay all costs, including employee and employer costs.

Disability retirement

In addition to regular retirement, PERA provides duty and nonduty disability retirement to its members. Members are eligible for duty disability, with 100 percent disability, from the first day of employment and are eligible for nonduty disability after vesting with five years of service credit.

Cost-of-living adjustment (COLA)

Retirees are eligible to receive a three percent COLA after being retired for two full calendar years, effective July 1 of the following year. Because the COLA is calculated on the calendar year, December 31 is a popular retirement date for PERA.

Return-to-work (RTW) provisions

Retirees may return to work for a PERA-affiliated employer after waiting out 90 consecutive calendar days from the date of retirement to reemployment. Reemployed retirees may receive a salary and a pension but not earn additional service credit. The employer must pay both the employer and employee shares of contributions on the salary earned by the reemployed retiree. There are approximately 2,100 reemployed state and municipal retirees.

As of May 31, 2009, the PERA had assets of $9.046 billion, down from a high of $13.3 billion on June 30, 2007 and up from a low of $7.2 billion on March 3, 2009. In the last 90 days, the fund's assets have increased 11 percent, the largest increase for a single quarter in the past 15 years. The actuarial assumed rate of investment is eight percent, which is the national norm;

however, currently the rate is about 7.2 percent. PERA's board policy is to finance the costs associated with current liabilities for existing PERA members — its unfunded accrued actuarial liability, or UAAL — over a period not to exceed 30 years. The June 30, 2008 valuation was 93 percent funded, with an aggregate funding period of 13 years. The recent significant negative market experience has put a strain on the future funded status and amortization period of the plan.

The PERA board has, or will, undertake several initiatives to improve the fund's performance and to ensure adequate coverage for current and future retirees.

Asset allocation

At its June 2009 board retreat, the board, with its investment consultants, will revisit its strategic asset allocation. While the board considered removing assets from the market several times during the recent market volatility, the investment policy rebalancing triggers are based on long-term investing targets rather than market timing. In the last 18 months, PERA has terminated 10 fund managers for poor performance.

Cash flow projection and benefit adequacy studies

The board will conduct an actuarial study on potential changes to the PERA's benefit plan structure based on cash flow projections. The in-depth study will be performed on all levels of benefits provided to its various membership groups as recommended by the PERA's actuaries. The study will entail research into length of service requirements, comparable state plan comparisons and social security versus non-social security coverage groups as well as associated costs. The board supports this comprehensive actuarial analysis in lieu of making wholesale changes to PERA's benefit structure.

Actuarial assumption changes

Results of PERA's recent four-year experience study determined that actuarial assumptions regarding terminations, pay increases and retirement rates warrant adjustments. The board is considering lowering the investment return assumption to 7.75 percent. However, any reduction in the actuarial assumed rate of investment return of eight percent will require a statutory contribution increase.

Representative Heaton noted that testimony before the investments oversight committee indicated that the state's pension plans have lost 30 to 40 percent of their value, and while there has been some recovery, it is not sufficient. That committee was also told that recession was not programmed into the models and assumptions used by the pension plans. On questions from Mr. Varela regarding the four-year smooth-out, Ms. Frederick said that based on the experience of the last year, the board wants to recognize losses more quickly. Representative Heaton asked about the cost to contributions to reduce the investment return from eight to 7.75 percent. Ms. Pittard said it would be approximately five percent.

Mr. Fulginiti pointed out that the RTW option may cost an affiliated public employer, but it does not endanger the fund. The employer must pay both the employer and employee share, and the employee share is nonrefundable to the employee.

Representative Heaton requested information on the number of RTW employees and their affiliated public employers.

Representative Stewart said that during the legislative session, people were discussing "spiking" — whereby an employee is promoted or otherwise given a significant pay raise to increase the final average salary calculation — as a problem with both retirement systems, though more so with PERA. She asked the effect of the loss of the antispiking provisions in House Bill 573. Ms. Pittard said that, statistically, spiking is not a concern for the association. PERA has a strict definition of salary, which does not include overtime, bonuses or unused sick or annual leave, and the retirement calculation is based on a 36-consecutive-month period. Mr. Arevalo noted that at its retreat, the board will hear the whole spectrum of considerations and evaluate all recommendations from the consultants.

Representative Berry initiated a discussion of the board's investment strategy. He pointed out that in the last year, there was no place to hide when the triggers for rebalancing were hit. He suggested that at the retreat, the board look at cash allocations, asset allocations, contributions and the constitutional limits on changing benefits.

Representative Stewart asked for information on the number of active and retired members in each plan.

<u>The ERB — Mr. Schatzman, general counsel</u> (written testimony)

The ERB has 63,000 plus active members, 31,000 plus retirees and 29,900 plus inactive members. "Inactive members" are those who have made no contributions within the last four months. There are 183 local administrative units (LAUs) in the ERB, including public schools, higher education, specialized schools and certain administrative agencies. The "regular" or defined benefit plan of the educational retirement system is a guaranteed monthly benefit based on final average compensation. The plan covers all members except those eligible members who elect to participate in the alternative retirement plan (ARP). The ARP is a monthly benefit based on contributions and investments earnings for an individual member's account. Certain college and university faculty and professional employees are eligible to participate on an optional basis. The ARP was created in 1991 for university faculty and professional employees; in 1999, the option was broadened to include community college faculty and professional employees.

Membership in the regular plan includes teachers, support staff and administrators — in short, all educational employees except those who participate in the ARP. Participation is mandatory for anyone who works more than .25 time. Retirement eligibility is 25 years, or the rule of 75 (age + service = 75) or age 65 with five years of service credit. Members retiring under the rule of 75 who are less than 60 years of age receive a reduced benefit. The monthly annuity is calculated as:

2.35 percent X years of service credit X the final average compensation (FAC). The FAC = five-consecutive-year period that results in the highest average salary.

Service credit is accrued each calendar quarter of contributing membership. It is granted for all four quarters, though many members work nine months per year. Unlike the PERA's 26 years, eight months, there is no maximum limit for the calculation of benefits. The calculation is 2.35 percent of *each* year of service credit. For example, 25 years of service provides 58.75 percent of the FAC; 30 years equals 70.50 percent and 40 years is 94 percent of the FAC. The annual retirement benefit increase is one-half of the cost of living index, with a maximum of four percent increase and a minimum of two percent increase. Because the COLA is paid on July 1, June 30 is the typical retirement date for the ERB.

The regular plan benefit is paid for life. A member may choose among three options. Option A is a full monthly retirement benefit with no survivor benefit. If the member dies before receiving benefits equal to the member's contribution, the balance is paid to a designated beneficiary. Option B is a reduced monthly benefit to provide a survivor benefit equal to the member's benefit. If the designated survivor predeceases the member, the member's benefit is increased ("pops-up") to the full monthly benefit. Option C is a reduced monthly benefit to provide a survivor with one-half of the member's benefit; also with a pop-up for the member if the survivor predeceases the member. To provide for a survivor, the monthly benefit reduction is based on the member's age at retirement. Pop-ups are subsidized by the educational retirement fund.

The ARP, a defined contribution plan, has 1,650 members, mostly at the University of New Mexico (UNM) and New Mexico State University (NMSU). Benefits are based on contributions and investment earnings. It is offered at New Mexico's colleges and universities only and was intended for faculty and professional employees who anticipated spending only a portion of their professional career in New Mexico. ARP members with seven years in the plan may switch to the regular plan as new members. While they do not get service credit for the past years, there is a reach-back for retirement. The ERB will be seeking proposals for other ARP plan options in the coming fiscal year.

There are approximately 1,340 RTW employees, most of whom are in traditional public schools; Albuquerque public schools make up about 65 percent of the RTW teachers. The balance of RTW participants are in charter schools, colleges and universities, state agencies and special schools. The RTW covers all ERB retirees, not just educators; however, it does not include retirees who work .25 time or less, earning $15,000 or less. The average RTW salary is approximately $43,800. Retirees must sit out 12 full months without being employed or contracted with by a LAU or affiliated entity and the RTW application must be approved by the ERB. Retirees may volunteer in unpaid positions without jeopardizing their wait period. Beginning July 1, 2009, LAUs must pay both employer and employee contributions to the ERB; this provision is similar to the PERA. The RTW program sunset was extended to January 1, 2022 in HB 573.

Selected ERB statistics as of June 30, 2008 include:

- average member salary and age: $37,347 and 45.9 years of age
- average service: 9.3 years
- FY 2008 retirees and average age at retirement:
    - 25 years of service: 715 retirees +/- 57 years old
    - rule of 75: 801 retirees +/- 62.5 years old
    - 65 plus five years of service credit: 243 retirees +/- 65.6 years old
    - total of 1,759 retirements
- FY 2009 retirements and applications to date: 1,879
- average monthly retirement benefit: $1,556
- ERB retiree payroll for FY 2008 was $582,653,000
- ERB total contributions for FY 2008 was $485,936,000, net of refunds
- FY 2008 difference ($96,717,000) paid from retirement fund
- 5,404 member contribution refunds in FY 2008 totaled $30,443,000

FY 2009 contribution rates are: employer – 11.65 percent; member – 7.9 percent = total 19.55 percent. House Bill 854 (Chapter 127) changes contribution rates for employees and employers for two years as follows:

Employee Salary ≤ $20,000
FY 2010: Employer – 12.40 percent, Member – 7.90 percent, Total – 20.30 percent
FY 2011: Employer – 13.15 percent, Member – 7.90 percent, Total – 21.05 percent
FY 2012: Employer – 13.90 percent, Member – 7.90 percent, Total – 21.80 percent

Employee Salary > $20,000
FY 2010: Employer – 10.90 percent, Member – 9.40 percent, Total – 20.30 percent
FY 2011: Employer – 11.65 percent, Member – 9.40 percent, Total – 21.05 percent
FY 2012: Employer – 13.90 percent, Member – 7.90 percent, Total – 21.80 percent

The estimated additional revenue from contribution increases (subject to revision based on changes in estimated employee salaries) are:
FY 2010: $20.4 million
FY 2011: $21.3 million
FY 2012: $22.2 million

The educational retirement fund has a balance of $6,638,605,459 as of April 30, 2009. The estimated May 30, 2009 fund balance is +/- $7,000,000,000, with an estimated monthly return of +/- five percent. The fund lost 28 percent of its value during the last year.

Mr. Bowyer noted that the number of retirees and inactive members were about the same and asked what effect that has on the fund. Mr. Schatzman said that a significant number of the inactive members are not vested. He added that as a trust, unclaimed contributions may revert to the state as escheats.

On questions from Representatives Varela and Heaton, Mr. Schatzman said he had heard rumors of a challenge to the PERA's increased employee contributions as a result of House Bill 573, but that he did not know if there would actually be a challenge. The ERB is a mature plan and as such pays out more than it collects in contributions. In response to Mr. Varela, Mr. Schatzman said that the ERB wants to survey its LAUs to determine whether the RTW is working.

Discussion then turned to the problems for ERB members because of language in House Bill 2 that specifies what constitutes a salary greater than $20,000. Representative Stewart pointed out that annualizing salaries of school employees, e.g., educational assistants, meant that they would have to contribute at the higher level. Ms. Aubel noted that the error occurred because the language was based on the calculation of full time for state employees, which is 2,080 hours. The LFC sent out a letter to ask that full time be defined for contribution purposes as it is defined in an LAU's budget.

<u>RHCA — Mr. Varela and Mr. Walsh</u>

The RHCA was created in 1990 and serves over 40,000 public employee retirees. The pre-medicare program serves 15,000 members and the medicare program serves 25,000 members. Following is a comparison of the two programs:

Pre-Medicare Program	Medicare Program
average age = 53	average age = 73
average cost = $5,950 annually	average cost = $2,640 annually
covered by three PPO plans: gold = $100 deductible; $1,000 OOP max silver = $400 deductible; $2,000 OOP max bronze = $800 deductible; $4,000 OOP max (OOP = out of pocket)	covered by traditional medicare supplement and medicare advantage plans: supp. (20,000 members) = higher premium, lower OOP advantage (5,000 members) = lower premium, higher OOP
comprehensive ℞ coverage = between $7.00 (generic) and $80.00 (nonformulary brand)	comprehensive ℞ coverage = between $7.00 (generic) and $80.00 (nonformulary)

Retirees must have at least five years of service credit with a participating entity to participate in the plan and receive the minimum subsidy. Retirees receive full subsidy after 20 years of service.

Market value of the fund was $136,028,472.70 in October 2008 and was $136,752,722.24 as of April 2009; however, in the months between those dates, the fund had substantial losses, reaching a low of $122,897,300.45 in February 2009. The RHCA invests through the state investment council, although it does hire advisors and actuaries. Its asset allocation is 60/40. House Bill 351 of the last session increased the employer/employee contribution rates. The increase, from the current 1.95 percent, is rolled out over a three-year period beginning in 2011. By July 1, 2013, the employer/employee contribution rate will be three percent. Two other solvency measures were included in House Bill 573. One measure requires persons purchasing service credit from the PERA or the ERB to also purchase service credit from the RHCA. The other measure requires RTW employees and their employers to contribute to the RHCA.

Issues identified for the July annual meeting include premium increases, plan design changes, selection of plans and carriers for medicare members and a review of other finance elements.

On questions from Representative Varela, Mr. Walsh said that the retiree health care fund is considered by the governmental accounting standards board (GASB) to be solvent until 2027, though the board uses a more conservative measure of 2018.

Mr. Bowyer asked if an employee may take the employee's contributions if the employee leaves a participating entity's employ. Mr. Walsh answered in the negative.

Representative Heaton indicated that by some accounts the RHCA was underfunded by $2.9 billion. Mr. Walsh agreed that the amount was the unfunded actuarially accrued liability as of June 30, 2008 but that it does not reflect insolvency, which is a different concept.

Representative Heaton also initiated a discussion of utilization patterns and systemic inefficiencies. For example, Representative Heaton discussed the push over the last decade to have more medicare beneficiaries use a health maintenance organization model through medicare advantage plans that have, according to some studies, shown higher administrative costs, lower provider payments and inefficiencies for medicare beneficiaries.

Mr. Varela said that one of the things the board will consider during its retreat is whether the authority should continue as a self-insured model.

Proposed Work Plan and Budget — Raúl Burciaga, staff

Mr. Burciaga presented a proposed work plan for the task force's consideration. After discussion, Mr. Bowyer moved and Mr. Varela seconded that consideration of defined contribution plans be stricken from the work plan. Members agreed that if the goal is to fix solvency problems, the task force will need actuarial information as soon as possible for quick, early analyses. With so many moving parts, it is difficult to know how to adjust to meet solvency and how to identify the gaps. Mr. Schatzman pointed out that states that have moved to defined contributions are moving back, and he proposed a third option of defined contribution with minimum guarantee. Ms. Aubel noted that the problem with getting early actuarial information is that actuaries want to use audited numbers; she suggested as an alternative to use estimates. Ms. Pittard informed the task force that the PERA is conducting its own actuarial study and said that anyone will have to wait until June 30 for second-quarter data, which would then have to go to the actuaries. Representative Heaton suggested that a course of action might be to make hypothetical assumptions and then devise recommendations that include all the working parts. Mr. Fulginiti remarked that there should be national models that could be used to measure the New Mexico plans. After further discussion, the task force agreed to have Mr. Burciaga wordsmith the item. The task force agreed to the November 11-12 date. On motion of Ms. Trujillo, seconded by Ms. Lewis, the work plan was adopted for editing and submission to the legislative council.

The next meeting of the task force will be August 10-11 in Room 307, State Capitol. The meeting will begin at 10:00 a.m. on August 10 and 9:00 a.m. on August 11.

There being no further business, the task force adjourned at 4:10 p.m.