

Fiscal impact reports (FIRs) are prepared by the Legislative Finance Committee (LFC) for standing finance committees of the NM Legislature. The LFC does not assume responsibility for the accuracy of these reports if they are used for other purposes.

Current FIRs (in HTML & Adobe PDF formats) are available on the NM Legislative Website (legis.state.nm.us). Adobe PDF versions include all attachments, whereas HTML versions may not. Previously issued FIRs and attachments may be obtained from the LFC in Suite 101 of the State Capitol Building North.

## FISCAL IMPACT REPORT

ORIGINAL DATE 2/8/10

SPONSOR King LAST UPDATED \_\_\_\_\_ HJM 55

SHORT TITLE Study Soundness of Judicial Retirement SB \_\_\_\_\_

ANALYST Aubel

### ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY10	FY11	FY12	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
<b>Total</b>		NFI				

(Parenthesis ( ) Indicate Expenditure Decreases)

### SOURCES OF INFORMATION

LFC Files

#### Response Received From

Administrative Office of the Courts (AOC)

#### No Response From

Public Employees Retirement Association (PERA)

### SUMMARY

#### Synopsis of Bill

House Joint Memorial 55 requests the Public Employees Retirement Association (PERA) and the Administrative Office of the Courts (AOC) study the actuarial soundness of the Judicial and Magistrate Retirement funds and prepare a solvency plan to ensure soundness.

This joint memorial requires that PERA and the AOC present their findings to the investment oversight committee no later than November 1, 2010.

### FISCAL IMPLICATIONS

AOC provides the following background:

PERA conducts an annual actuarial valuation of JRA and MRA as part of the overall PERA fund actuarial valuation on June 30 of every year. PERA's actuary, Gabriel, Roeder, Smith and Company (GRS), has repeatedly indicated that the reliance of docket fees to fund retirement benefits is insufficient to amortize the unfunded actuarial accrued liability. There is a poor correlation between docket fee revenue and judicial payroll.

In the June 30, 2009 PERA Actuarial Valuation Report, GRS recommended that all employer contributions be related to payroll and that serious action be taken to mitigate these two funds deficiencies within the next couple of years. In addition, this was the first year that GRS indicated that the MRA is currently in a negative non-investment cash flow (benefits minus contributions) of over \$1 million and that the fund will become insolvent (be unable to meet cash flow) in 20 to 25 years if the contribution deficiency is not addressed.

Because the actuarial study is already conducted annually, no additional funding is required to implement this joint memorial. It is assumed that the resources used by AOC and PERA in developing the plan could be achieved within current operating budgets. Thus, there is no fiscal impact for the study.

## **SIGNIFICANT ISSUES**

### Judicial Retirement Plan

The statutory obligations of the Judicial Retirement Plan is to provide pension payments to current and future retired judges, vested former judges and survivor pension beneficiaries. The sources of funding include:

- 9% of salary by members (includes 1.5% employee-employer contribution shift for FY10 and FY11 pursuant to Laws 2009, Chapter 127.)
- 10.5% of salary by employers (includes 1.5% employee-employer contribution shift for FY10 and FY11 pursuant to Laws 2009, Chapter 127.)
- A portion of district court civil docket fees (\$38)
- Investment earnings on Judicial Retirement fund assets

As of June 30, 2009, the total actuarial obligation of the fund was \$120.8 million and the actuarial value of assets was only \$73.1 million, producing an unfunded accrual accrued liability (UAAL) of \$47.7 million. The funded ratio (ratio of assets to obligations) was 60.5 percent. The minimum industry standard is 80 percent. The current contribution is insufficient to amortize the UAAL, which means the obligation will not be paid given all actuarial assumptions hold. This equates to an infinite funding period; the industry minimum is 30 years.

In order to amortize the UAAL over the standard 30 years, the contribution would have to be raised from the current statutory contributions of 37.66 percent (based on docket fees for 2008/2009 fiscal year contributions) to 53.49 percent. Comment C in the 2009 actuarial valuation concluded: “In the absence of gains, the funded condition of this plan will deteriorate unless the contribution issue is addressed.”

To address the under funding of the judicial plan, Laws 2005, Chapter 246, increased the employee and employer contributions over a two-year period to 7.5 percent and 12 percent, respectively, as of FY07. A minimum age requirement was set at 55, eliminating the early retirement provisions that allowed retirement between the ages of 50 to 60 with 18 years of service credit. The final average salary calculation was adjusted to reduce plan costs for members entering the system after July 1, 2005.

These plan changes have been apparently unsuccessful in addressing the solvency issue of the plan. It appears that continuing to base partial funding on docket fees rather than 100 percent on judicial payroll remains a key issue as indicated by PERA’s actuaries.

Magistrate Retirement Plan

The statutory obligations of the Magistrate Retirement Plan is to provide pension payments to current and future retired magistrates, vested former magistrates and survivor pension beneficiaries. The sources of funding include:

- 9% of salary by members (includes 1.5% employee-employer contribution shift for FY10 and FY11 pursuant to Laws 2009, Chapter 127.)
- 9.5% of salary by employers (includes 1.5% employee-employer contribution shift for FY10 and FY11 pursuant to Laws 2009, Chapter 127.)
- A portion of district court civil docket fees (\$38)
- Investment earnings on Magistrate Retirement fund assets

As of June 30, 2009, the total actuarial obligation of the fund was \$47.6 million and the actuarial value of assets was only \$31.5 million, producing an unfunded accrual accrued liability (UAAL) of \$16.0 million. The funded ratio (ratio of assets to obligations) was 66.3 percent. The minimum industry standard is 80 percent. Not only is the current contribution insufficient to amortize the UAAL, the contributions are not even covering the normal cost of the plan. Just to keep up with funding the pension obligations being earned by current members, the plan needs 35.36 percent but the total contributions are only 32.67 percent. The annual negative cash flow is about \$1 million. This means, given all actuarial assumptions hold, the plan will continue to deteriorate.

In order to pay the normal cost and amortize the UAAL over the standard 30 years, the contribution would have to be raised from the current statutory contributions of 32.67 percent (based on docket fees for 2008/2009 fiscal year contributions) to 55.30 percent. Comment G in the 2009 actuarial valuation concluded:

If future investment income is, on average, sufficient to cover the future growth of the (\$1 million shortfall), this fund will become insolvent (be unable to meet cash flow) in 20 to 25 years if the contribution deficiency is not addressed. Only two years ago, this fund was 100.7% funded. In two short years it has dropped to 66.3%.

To address the under funding of the magistrate plan, Laws 2005, Chapter 247, increased the employee and employer contributions over a two-year period to 7.5 percent and 11 percent, respectively, as of FY07.

These plan changes have been apparently unsuccessful in addressing the solvency issue of the plan. It appears that continuing to base partial funding on docket fees rather than 100 percent on judicial payroll remains a key issue as indicated by PERA's actuaries.

Other plan changes affected the actuarial health of the both plans, including moving members from one plan to another and reducing the retirement eligibility requirement for the MRA. These provisions would need to be reviewed as part of the study.

**PERFORMANCE IMPLICATIONS**

Two years of investment losses (2008 and 2009) have not helped these plans. Returns above the actuarial return of 8 percent will have a positive impact, although it is unlikely that returns alone can place these plans on the path to solvency.

**RELATIONSHIP**

Relates to Senate Bill 246 that proposes another employee-employer contribution shift for PERA plans. PERA notes that this will have a negative actuarial impact on the funds.

**TECHNICAL ISSUES**

The June 30, 2010, valuation will most likely not be completed until October 2010 at the earliest, which may leave insufficient time for PERA and OAC to review and prepare proposals by November 1. However, both agencies seem prepared to move forward with the study. In addition, the task force convened by Laws 2009, Chapter 288, to study solvency issues relating to PERA, the Education Retirement Act, and the Retiree Health Care Authority will undoubtedly be reviewing the same issues for JRA and MRA as part of their activities.

**WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL**

The plans will still be reviewed by the task force convened pursuant to Laws 2009, Chapter 288, but the resulting proposals for JRA and MRA may not receive the heightened scrutiny as would be provided by a focused group.

MA/mt