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

ORIGINAL DATE 01/25/10
SPONSOR Smith **LAST UPDATED** 02/14/10 **HB**

SHORT TITLE Delay Educational Retirement Contributions **SB** 91

ANALYST Aubel

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY10	FY11	FY12	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total		($18,292.0)	See fiscal impact	($18,292.0)	Nonrecurring	ERB-affiliated Employers

(Parenthesis ( ) Indicate Expenditure Decreases)

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY10	**FY11**	**FY12**		
	($18,292.0)	See fiscal impact	Nonrecurring	ERB

(Parenthesis ( ) Indicate Revenue Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Educational Retirement Board (ERB)
Higher Education Department (HED)

SUMMARY

Synopsis of Bill

Senate Bill 91 is a Legislative Finance Committee-sponsored bill that delays the 0.75 percent increase scheduled for FY11 in the employer contributions to the Education Retirement Board (ERB) by one year.

The effective date of the bill is July 1, 2010.

FISCAL IMPLICATIONS

Operating Budget-FY11

Laws 2005, Chapter 273, increased the employer contribution rate 0.75 percent annually from FY06 through FY12 to a final 13.9 percent (Attachment A – Table A.) FY11 represents the sixth year of this schedule. Based on the appropriation included in Laws 2009, Chapter 124 (Attachment A – Table B), going forward each of these 0.75 percent increments equates to an approximate additional $18.3 million general fund appropriation. SB91 proposes to suspend the 0.75 percent increase for FY11, which represents an estimated $18.3 million reduction in the obligation for the ERB-affiliated employers for one year.

Neither the LFC nor the Executive budget recommendations for FY11 include funding for this 0.75 percent employer contribution increase. Thus, without this bill or similar legislation, the ERB-affiliates would have to absorb the increase obligated through current statute totaling about $18.3 million within the FY11 operating budgets, or additional general fund would need to be appropriated for this purpose.

Operating Budget-FY12

This bill has a one-year impact. The bill preserves current statute that provides the 0.75 percent contribution increase pursuant to Laws 2005, Chapter 273, will continue in FY12. In addition, pursuant to Laws 2009, Chapter 127, the 1.5 percent employee-employer swap will sunset June 30, 2011. Thus, under statutory provisions, the employer contribution rate will increase a total of 2.25 percent from FY11 to FY12 (0.75% + 1.5%). As shown in Attachment A - Table D, the rate would increase from 10.9 percent to 13.15 percent.

Revenue to ERB

The following discussion provides more detail by comparing the employer contributions set under current statute to that which would occur as proposed by this bill. Using the FY10 appropriation of $18.3 million and assuming zero salary increases, Table 1 shows the estimated incremental and cumulative funding requirements under Scenario 1 – the original funding schedule – and under Scenario 2 – as contemplated by this bill. These numbers represent revenue to ERB.

Table 1 – Revenue to ERB Due to Annual Employer Contribution Increase

Scenario 1 - Current Statute	**FY11**	**FY12**	**FY13**
FY11	$18,292	$18,292	$18,292
FY12		$18,292	$18,292
FY13			N/A
Total Increase Revenue	$18,292	$36,584	$36,584
Scenario 2 – SB18	**FY11**	**FY12**	**FY13**
FY11	$0	$0	$0
FY12		$18,292	$18,292
FY13			$18,292
Total Increase Revenue	$0	$18,292	$36,584
DIFFERENCE	($18,292)	($18,292)	

ERB has noted the fiscal impact of delaying the incremental $18.3 million revenue increase for FY11 until FY12 represents an opportunity cost to the fund that would depend on investment returns over this period. The ERB analysis estimates a reduction in the Market Value of Assets by $177 million on a projected total fund value of $17.4 billion by 2030.

Actuarial Impact of One-Year Delay

Table 2 shows the projected impact of delaying the employer contribution increase on actuarial solvency measures, the funded ratio (actuarial value of assets compared to the actuarial value of liabilities) and funding period (the amount of time estimated to pay off the unfunded liability). The impact appears deminimus.

Table 2 – Impact on Actuarial Solvency Measures*

Fiscal Year	Without One-Year Delay		With One-Year Delay	
	Funded Ratio	**Funding Period**	**Funded Ratio**	**Funding Period**
FY10	67.3%	48.7	67.3%	48.7
FY11 (delay)	63.3%	55.1	63.3%	94.3
FY12	59.3%	61.5	59.1%	infinite
FY13	54.9%	infinite	54.6%	infinite
FY24	53.5%	infinite	53%	infinite
FY25	53.6%	113.8	53.1%	186.4
FY38	61%	34.2	60.3%	35.6

*Source: ERB

Minimum industry standards require 80 percent for the funded ratio and 30 years for the funding period. The bill's impact primarily influences the funding period, extending the fund's infinite funding status by one year in FY12. In both cases the indicators fall substantially below industry standards, portraying a situation where the obligations promised to current retirees and active members are being pushed out to future generations to fulfill. Delaying the employer contribution increase for one year will not substantially alter this picture. However, deviations from assumptions, such as over or under performing the 8 percent assumed rate of investment return, could materially impact this dynamic.

SIGNIFICANT ISSUES

Due to concerns regarding fund solvency, Laws 2005, Chapter 273, incrementally raised the employee rate to 7.9 percent by FY09 and the employer contribution rate by 0.75 percent annually from the statutory rate of 8.65 percent in FY05 to 13.9 percent by FY12. The bill maintains the rate beginning July 1, 2009 through June 30, 2011, and then resumes the 0.75 percent annual increase beginning July 1, 2011. Thus, the original rates would take full effect by FY13, one year later than originally scheduled.

As part of balancing the budget, neither the LFC nor the Executive recommendations funded this increase for FY11 in public education or higher education institutions.

As shown in Attachment A - Table D, the employer contribution rate would increase from 10.9 percent in FY11 to 13.15 percent for FY12.

The Legislature attempted to pre-fund the annual ERB increase though an accelerated contribution appropriation as a “rainy day” measure twice, once in Laws 2006, Chapter 109—which was vetoed—and Laws 2007, Chapter 28—which was also vetoed.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Not passing this bill will create an unfunded mandate for paying the 0.75 percent increase in employer contributions for ERB-affiliates totaling about $18.3 million.

MA/svb

Attachment A

Table A – Laws 2005, Chapter 273

Fiscal year	Employee Contribution Rate	Employer Contribution Rate	Incremental Change in Employer Rate
FY05	7.6%	8.65%	
FY06	7.675%	9.4%	0.75%
FY07	7.75%	10.15%	0.75%
FY08	7.825%	10.9%	0.75%
FY09	7.9%	11.65%	0.75%
FY10	7.9%	12.4%	0.75%
FY11	7.9%	13.15%	0.75%
FY12	7.9%	13.9%	0.75%

Table B – Fiscal Impact of 0.75% increase in Employer Contribution Rate for FY10 (in thousands)

Public School Support *	
Program Costs	$12,073.2
Transportation	$194.8
Higher Education**	$6,024
TOTAL	**$18,292.0**

*Source: Public Education Department

**Source: Laws 2009, Chapter 124, page 188

Table C – Current Rates: Laws 2005, Chapter 273 and Temporary 1.5% Employer-Employee Swap (Laws 2009, Chapter 127)

Fiscal year	Employee Contribution Rate > $20,000	Employer Contribution Rate	Incremental Change in Employer Rate
FY10*	7.9%+1.5% = 9.4%%	12.4% - 1.5% = 10.9%	0.75%
FY11*	7.9%+1.5% = 9.4%	13.15% - 1.5% = 11.65%	0.75%
FY12	7.9%	13.9%	0.75%

*Laws 2009, Chapter 127

Table D – Effective Combined Rate Changes*

Fiscal Year	Employee>$20,000	Employer
*FY10	9.4%	10.9%
Effective Rates Proposed by Senate Bill 91		
*FY11	9.4%	10.9%
FY12	7.9% (-1.5%)	13.15% (+1.5% +0.75%)
FY13	7.9*	13.9%

*Includes 1.5% employee-employer swap enacted by Laws 2009, Chapter 127.