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

**ORIGINAL DATE** 01/31/11
**SPONSOR** Varela **LAST UPDATED** 01/10/11 **HB** 129/aHEC

**SHORT TITLE** Returning Educational Retiree Payments **SB**

**ANALYST** Aubel/Gudgel

## ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in millions*

| | FY11 | FY12 | FY13 | 3 Year Total Cost | Recurring or Non-Rec | Fund Affected |
|---|---|---|---|---|---|---|
| **RTW Employee Contribution Shift** | | *($4.6)-($6.5) | *($4.6)-($5.5) | *($9.2)-($12.0) | Recurring | General Fund |

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

Relates to Senate Bill 248, Senate Bill 265 and House Bill 133
Relates to Appropriation in the General Appropriation Act

House Bill 129 is a bill sponsored by the Legislative Finance Committee.

## SOURCES OF INFORMATION
LFC Files

Responses Received From
Educational Retirement Board (ERB)
Children, Youth and Family Department (CYFD)
Higher Education Department (HED)
Public Education Department (PED)

## SUMMARY

Synopsis of HEC Amendment

The House Education Committee amendment adds language that clarifies that the payments made by a retired member pursuant to the bill are non-refundable.

Synopsis of Original Bill

House Bill 129 changes current pension contribution requirements for return-to-work (RTW) employees under the Education Retirement Act. Currently, ERB employers pay both employee and employer contributions for RTW employees. HB 129 shifts responsibility for the employee's contribution to the employee – as is currently structured for "grandfathered" RTW employees working under the Public Employees Retirement Association (PERA).

## FISCAL IMPLICATIONS

ERB reports about 1,300 RTW employees were employed during FY10, about 1,100 working at public schools and 200 at institutions of higher education. Employers were responsible for paying employee contributions at a rate of 9.4 percent, at a total cost of $5.5 million. Shifting the responsibility to the employees allows funding to be reduced by the employee statutory contribution amount, generating a recurring savings to the general fund. Actual savings would depend on the number of RTW employees and the contribution rate in effect over this period.

The current employee statutory rate returns to 7.9 percent in FY12. Both the Executive and LFC budget proposals assume the continuation of the 1.5 percent contribution shift enacted in Laws 2009, 2nd Special Session, Chapter 129, at least through FY12. The LFC-sponsored bill, Senate Bill 248, would make this shift permanent. In addition, SB 248 proposes an additional one-time 1.75 percent employer-to-employee shift for FY12 as part of the package to balance the state's budget. Thus, the various proposals produce the range of contribution rates and their associated potential savings as depicted in Table 1. These savings would be recurring.

**Table 1 – Potential Savings Due to House Bill 129**
**(in millions)**

| Employee Contribution Rate | FY12 | FY13 | Total Potential Savings |
|---|---|---|---|
| Current Statute: 7.9% | $4.6 | $4.6 | $9.2 |
| +1.5% Shift 9.4% | $5.5 | $5.5* | $11.0* |
| +1.75%Shift 11.15% | $6.5 | $5.5* | $12.0* |

*Assumes the 1.5% employer-employee shift remains beyond FY11.

The 9.4 percent employee contribution includes the base 7.9 percent plus the temporary 1.5 contribution swap that is scheduled to sunset by July 1, 2011. The estimated fiscal impact of $5.5 million general fund savings assumes Senate Bill 248, which makes the 1.5 percent shift permanent, passes. If that bill, or a similar bill, does not extend the 1.5 percent contributions shift beyond July 1, 2011, the general funds savings would be reduced by about $900 thousand to equate to the 7.9 percent rate.

The LFC budget recommendation for both public school support and higher education assume shifting responsibility for making the total employee contribution for retired members employed pursuant to the RTW program from the employer to the employee. The public school support budget was reduced by $4.9 million general fund, and the general fund appropriations for higher education institutions were reduced by a total of $590 thousand.

Thus, if this or similar legislation is not enacted, then either additional general fund appropriations would need to be made to cover the unfunded cost to the employers, increasing the budget deficit, or the affected employers would need to absorb the added expense of making the employee contributions. This would reduce funding for other areas of the education budgets.

CYFD notes that the department only has RTW employees in JJS Education that fit this criteria and concluded the budget savings would be minimal.

## SIGNIFICANT ISSUES

Current estimates show state revenues will be short by over $200 million. House Bill 129 is a Legislative Finance Committee sponsored bill as part of a solvency package to produce a balance state budget as required by the New Mexico Constitution.

Originally, the ERB RTW program was scheduled to sunset in FY12. Section 22-11-25.1 (E) NMSA 1978 (Laws 2009, Chapter 288) extended the sunset date to 2022 and specified that an ERB employer employing a retired member (employee) pursuant to the RTW program shall make both the employee contribution and the employer contribution. Prior to this legislation, the employer was required to make only the employer contribution; member contributions were not being made by either the employer or employee. This lack of employee contributions was detrimental to ERB pension solvency. The 2010 law requiring the employer to also make the employee contribution for RTW employees was expected to increase fund solvency and bring the program into contribution parity with the PERA RTW program, which at that time also required the employers make both employee and employer contributions.

Laws 2010, Chapter 18, (Section 10-11-8 NMSA 1978) effectively eliminated the PERA RTW program beginning July 1, 2010. Retired members employed pursuant to the RTW program prior to July 1, 2010 were grandfathered into the PERA's RTW program; however, beginning July 1, 2010, grandfathered members were required to begin making the employee contribution. This legislation did not impact the ERB RTW program. House Bill 129 strives to bring the two RTW programs into parity with respect to the employee contribution.

ERB notes that HB 129 will not impact other ERB retirees who have returned to work under other rules that allow a person to retire and return to work without suspending his or her pension and without a "wait out" period (currently set at 12 months for the formal RTW program). These exemptions to the regular RTW program include two ERB exemptions that allow a retiree to return to work and 1) earn up to $15,000 or 2) a salary equal to quarter time for that position. In addition, PERA/ERB rules allow a PERA retiree to work for an ERB-affiliate without regard to a salary cap or wait out period. These exemptions total almost 1,200 retirees as noted in Table 2.

**Table 2 – Profile of ERB and PERA Retirees Who Have Returned to Work at an ERB-Affiliate**

| | RTW | <$15k | Quarter Time | PERA RTW |
|---|---|---|---|---|
| No. of Members | 1302 | 454 | 314 | 412 |
| Average Monthly Benefit | $ 2,436.02 | $ 1,921.60 | $ 3,597.11 | NA |
| Average Wages FY10 | $ 45,101.99 | $ 7,456.10 | $ 15,202.40 | $ 30,662.28 |
| Average Years between RTW | 2.64 | 1.96 | 1.95 | NA |
| Average Years on RTW | 4.42 | 4.19 | 3.99 | NA |
| K-12 | 1091 | 237 | 96 | |
| Higher Ed | 200 | 214 | 217 | |
| State Agency | 11 | 3 | 1 | |

Source: ERB

ERB reports that the number of RTW program retiree participants is fairly steady with 1,343 in FY08 and 1,473 in FY09. However, the average salary per RTW retiree has increased from $39,079.42 in FY08.

ERB includes a final comment regarding the issue of non-refundable RTW employee contributions:

> "…it should be made clear that the employee is not entitled to a refund of any of the contributions made while they are participating in the RTW program. There have been legal challenges to similar employee contributions for PERA RTW participants regarding the return of post-retirement contributions by RTW employee."

The issue was that the employee making the contribution did not receive any benefit, i.e., service credit. However, a case brought by Albuquerque police officers in state court (Archunde v PERA) was dismissed on the concept that to be able to receive a retirement benefit and go back to work and also receive a salary *was* a benefit. ERB proposes an amendment to make it clear that the contributions are nonrefundable.

**ADMINISTRATIVE IMPLICATIONS**

ERB provides the following summary for administrative implications:

> ERB would have to modify its retirement software and accounting programs to properly process employee contributions for RTW retiree participants. The cost is unknown but should be covered in ERB's retirement system software maintenance contract at no additional cost. In addition, ERB Local Administrative Units would have to reprogram their computer systems to be able to properly report this new category of employee contributions to the ERB fund.

**RELATIONSHIP**

House Bill 129 relates to Senate Bill 248, which makes the 1.5 employer-to-employee contribution shift permanent and adds a one-time 1.75 percent contribution shift for FY12.

House Bill 129 relates to House Bill 133, which is an Investment Oversight Committee sponsored bill that delays the current statutory increase in the employer rate of 1.5 percent set for 0.75 percent in FY12 and 0.75 percent for FY13 over a six-year period, ending at 13.9 percent for all employees, regardless of salary, by FY17.

House Bill 129 relates to Senate Bill 265, which is the ERB proposal to increase contribution rates for both employees and employers over a six-year period.

**TECHNICAL ISSUES**

ERB proposes the following amendment to clarify that the contributions are nonrefundable to the RTW employee:

> A suggestion on Page 3, line 2 to **delete** "an" and **add** "a nonrefundable"

**OTHER SUBSTANTIVE ISSUES**

Testimony presented to support extending the ERB RTW program during hearings for Laws 2009, Chapter 288, primarily emphasized the continuing need for schools to tap the pool of retirees for "hard-to-fill" positions, such as math and special needs teachers. However, the following profile of positions filled by RTW employees suggests that the program extends beyond this intent and may be allowing "double dipping" to the detriment of providing new job opportunities for the current generation of potential employees.

**Table 3 – Profile of Positions Filled by Retirees**

| Position Type | RTW | <$15,000 | Quarter Time | PERA RTW |
|---|---|---|---|---|
| Administrator | 170 | 14 | 11 | 0 |
| Non-Certified | 181 | 128 | 23 | 0 |
| Other Certified | 174 | 31 | 34 | 0 |
| Teacher | 718 | 143 | 54 | 0 |
| Unknown | 0 | 11 | 129 | 473 |
| Total | 1243 | 327 | 251 | 473 |

Source: ERB

PED suggests while HB 129 could allow for a budget savings for the ERA employer, "the contributions would be transferred to the employee, which could present an obstacle in recruiting and hiring valuable retired educators." However, it is unclear whether having RTW employees pick up the employee share of the pension contribution represents a significant deterrent to returning to work because the RTW employee still retains his or her pensions and gets a salary. The more significant impact to the ability to hire and retain valuable retired educators would occur if the RTW program was changed where the RTW employee had to suspend his or her pension before coming back to work.

**ALTERNATIVES**

HED proposes the following alternative:

> Conduct a cost study analysis of retirement benefits that will address changes to employee and/or retiree contributions. Based on the findings from both short term and long term results, construct a new formula to calculate benefits and contributions that are best feasible by both the retiree and the employer.

While the idea has merit, it is unlikely that such a cost study analysis could be conducted in the time frame needed to address the FY12 deficit as proposed under HB 129.

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

Employers will continue to be responsible for making the total member contribution for retired members employed pursuant to the RTW program. Either the affected employers would need to absorb the extra expense by making cuts elsewhere in their budgets, or an additional $5.5 million general fund appropriation may have to be made to cover the cost, increasing the budget deficit by that amount.

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