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

			02/03/11		
		ORIGINAL DATE	02/22/11*		
SPONSOR	Stewart	**LAST UPDATED**	03/07/11	**HB**	133
SHORT TITLE	Delay Educational Retirement Contributions			**SB**	
				ANALYST	Aubel

*This change clarifies that the 1.5% contribution shift sunsets for the employee but the bill does require the employer to replace that 1.5% contribution over six years rather than all at once in FY12. This is a semantic change and does not change the fiscal analysis.

REVENUE COMPARED TO CURRENT STATUTE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY11	**FY12**	**FY13**		
	($47,023.6)	($53,741.3)	Nonrecurring	ERB

(Parenthesis ( ) Indicate Revenue Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT* (dollars in thousands)

Compared to:	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Statute		($47,023.6)	($53,741.3)	($141,070.8)	Nonrecurring	All funds/89% General Fund
FY11		$10,794.6			Recurring	All funds/89% General Fund

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

Relates to Appropriation in the General Appropriation Act
Conflicts with SB 248/SPACS/aSFC, SB 265, SB 303 and HB 628/HAFCS

SOURCES OF INFORMATION
LFC Files

House Bill 133 is sponsored by the Investment Oversight Committee.

<u>Responses Received From</u>
Educational Retirement Board (ERB)
Higher Education Department (HED)
University of New Mexico (UNM)

SUMMARY

Synopsis of Bill

House Bill 133 amends Section 21-11-21 NMSA 1978. This legislation delays both the employer replacement of the 1.5 percent employer-to-employee contribution shift and the 1.5 percent employer increase currently scheduled for local administrative unit members (employers) of the Educational Retirement Board (ERB) and spreads the total 3 percent employer increase over six years. The bill changes the schedule of employer contributions, beginning in FY12, by starting at 11.4 percent in FY12 (the FY11 rate of 10.9 percent for employees>$20,000 plus 0.5 percent) and adds a contribution rate increase of 0.5 percent annually through FY17, ultimately reaching the final 13.9 percent employer contribution originally scheduled to occur in FY13.

Effective date for provisions of this act would be July 1, 2011.

FISCAL IMPLICATIONS

Compared to Statutory Rates Set for July 1, 2011

The bill does not change the statutory employee rate, which is scheduled to revert to 7.9 percent in FY12 for all employees, regardless of salary.

The current employer statutory rate for ERB as of July 1, 2011 is 13.15 percent for all employees regardless of salary level. This 13.15 percent would generate about $353.3 million employer contributions (revenues) in FY12, based on the ERB reported total salaries of $2.7 billion for FY10. For FY13, the 13.9 employer contribution would equate to about $373.5 million. House Bill 133, which would lower the rate to 11.4 percent in FY12 and increase the rate by 0.5 percent annually until FY17, would reduce the revenue coming into ERB by the following schedule:

Table 1 – Employer (ER) Contribution Revenue Comparison

	Current Statute ER%	ER Contribution	HB133		
FY12	0.1315	$ 353,348,865.06	$ 306,325,251.84	11.4%	$ (47,023,613.22)
FY13	0.139	$ 373,501,842.16	$ 319,760,569.91	11.9%	$ (53,741,272.25)
FY14		$ 373,501,842.16	$ 333,195,887.97	12.4%	$ (40,305,954.19)
FY15		$ 373,501,842.16	$ 346,631,206.03	12.9%	$ (26,870,636.13)
FY16		$ 373,501,842.16	$ 360,066,524.10	13.4%	$ (13,435,318.06)
FY17		$ 373,501,842.16	$ 373,501,842.16	13.9%	$ -
					$ (181,376,793.85)

Thus, from the point of view of ERB, the bill would reduce revenues coming in until the employer contribution rate matched the statutory rate of 13.9 percent in FY17. A secondary fiscal impact accrues due to the lost opportunity cost of not have these revenues earning investment returns of an expected 7.75 percent long term rate. ERB has not received the requested actuarial impact of the altered revenue stream over this six-year period but notes that this change will undoubtedly increase the unfunded accrued actuarial liability (UAAL). Thus, pension solvency is reduced under this plan in the short term but the bill maintains the 13.9 percent over the longer term, which will improve pension solvency.

The employee rate set at 7.9 percent as of July 1, 2011 is not changed under HB133 so would not generate a fiscal impact from the viewpoint of comparing the bill to statute.

The employer revenue to ERB represents operational expenses to the ERB employers. From the perspective of comparing what the employers would pay under this bill to that they would pay under current statute, all funding sources would be reduced by the equivalent amount. Using the 89 percent general fund proportion from the FY12 1% Table, this represents about a $41 million reduction in general fund expenditure for public education and higher education than what occur if no legislation is passed to change the effective rates that begin July 1, 2011.

The Higher Education Department comments on this issue as follows:

> Delaying educational retirement contributions for New Mexico's public postsecondary institution budgets might be preferable to requiring institutions to pay the scheduled increased employer contribution to the ERB on behalf of employees. Without additional General Fund support for this purpose, HB133 provides a possible alternative to employee layoffs, furloughs or self-imposed vacancy savings which may result in reduced operations.

Compared to FY11 Operating Budget

However, when viewed from the perspective of incremental budgeting, that is, from how much the employers will have to pay in FY12 when compared to operational expenses incurred for FY11, there is a positive fiscal impact of about $10.8 million, of which about 89 percent is general fund.

Table 2 – Employer Contribution Difference FY11/FY12 Under HB133

DIFF FY11/SB133	Employer Contribution FY12
$ 295,530,612.93	FY11
$ 306,325,251.84	FY12/HB133
$ 10,794,638.91	more needed over FY11 in FY12

A complete schedule compared to FY11 employer contribution rate is shown in Table 3, which compares the contributions valued by HB133 to those that would occur if the current FY11 rates were implemented, which would keep the 1.5 percent contribution shift and delay the two 0.75 percent employer increases. While showing the FY12 fiscal impact due to HB133 has merit, it should be noted that this scenario through FY17 is unlikely given apparent legislative intent to address pension solvency.

Table 3 – Employer Contribution Difference to FY11 Operating Budget through FY17

FY11 ER Contribution	HB133		
$ 295,530,612.93	$ 306,325,251.84	11.4%	$ 10,794,638.91
$ 295,530,612.93	$ 319,760,569.91	11.9%	$ 24,229,956.98
$ 295,530,612.93	$ 333,195,887.97	12.4%	$ 37,665,275.04
$ 295,530,612.93	$ 346,631,206.03	12.9%	$ 51,100,593.10
$ 295,530,612.93	$ 360,066,524.10	13.4%	$ 64,535,911.17
$ 295,530,612.93	$ 373,501,842.16	13.9%	$ 77,971,229.23
			$ 266,297,604.43

The primary point of this discussion is that the current version of the General Appropriations Act does not incorporate any incremental increase in the education operational budgets to pay for any additional employer ERB pension contributions in FY12. No appropriation is included in the bill to cover the cost. Thus, either the employers would have to absorb this additional cost of $10.8 million by reducing expenditures elsewhere or additional funding would need to be provided for FY12.

SIGNIFICANT ISSUES

Laws 2005, Chapter 273 implemented a schedule of employee and employer contribution increases to improve the funded status of the ERB fund, including a seven-year annual incremental increase of 0.75 percent for ERB employers ending at a final rate of 13.9 percent in FY12. It should be noted that Senate Bill 181, as originally drafted, implemented a four-year schedule of 0.75 percent increases ending at in FY09 at 11.65 percent. The additional 3 percent employer contribution, going from 8.65 percent to 11.65 percent, met ERB's actuarial recommendation designed to address solvency concerns at that time. A House Floor Amendment increased the schedule an additional three years to a final 13.9 percent, presumably to add a "cushion" for the educational plan to improve funded status.

Table 4 – Laws 2005, Chapter 273 (Senate Bill 181)

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%

Various changes in the statutory rates over the last two years have altered this original schedule. Laws 2009, Chapter 126 initiated a two-year 1.5 percent contributions shift from the employer to the employee as a solvency measure to produce a balanced state budget. Then, Laws 2010, Chapter 67 (Senate Bill 91), delayed the 0.75 percent employer increase scheduled for FY11 to FY12 and the final 0.75 percent employer increase to FY13.

Thus, the culmination of these three pieces of legislation, if left intact, produces a 2.25 percent increase in the employer ERB contribution effective July 1, 2011: 1.5 percent due to the sunset of the employee-employer shift for those making over $20,000 and the 0.75 percent employer increase that had been delayed by one year. The rate would go from 10.9 percent for those making over $20,000, and from 12.4 percent for those making $20,000 or less, to 13.15 percent for all employees. In FY13, the rate would go from 13.15 percent to the final 13.9 percent.

HB 133 allows the sunset of the 1.5 percent contribution shift for the employee and keeps the two 0.75 percent employer increases, but spreads the implementation of the contribution changes over six years rather than having them implemented more abruptly over the next two.

The current estimated revenue shortfall for FY12 ranges from the LFC projection of about $215 million to the executive's projection, based on differing assumptions, of $410.2 million. This shortfall will require additional solvency measures for FY12 to balance the state's budget as required by the New Mexico Constitution.

Thus, through this bill the Investment Oversight Committee strove to balance the issue of state solvency, by reducing the fiscal impact of contribution increases -- particularly for FY12 -- with ERB's pension solvency.

PERFORMANCE IMPLICATIONS

ERB notes that the reduced revenue may negatively impact the fund's ability to generate its expected 7.75 percent investment return.

ADMINISTRATIVE IMPLICATIONS

ERB notes that the bill will require ERB reprogram its retirement information system to adjust the employer's' contribution rate but maintains that the cost is minimal and would be paid out of the ERB's system maintenance contract with the software vendor.

CONFLICT

Conflicts with HB 628/HAFCS, which supports the contributions funded in the General Appropriations Act.
Conflicts with SB 248, which contains a different schedule of changes in employer contributions.
Conflicts with SB 265, which contains a different schedule of changes in employer contributions.
Conflicts with SB 303, which contains plan changes for both ERB and PERA.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Unless this or similar legislation to revise the current statutory rates is enacted, ERB employers will be facing a significant jump in pension contributions. Either additional funding will need to be provided to cover the cost or significant reductions in the operating budgets would occur elsewhere.

MA/mew:svb:bym