FISCAL IMPACT REPORT

SPONSOR	Sens. Stefanics and Trujillo/Reps. Martinez, A., Garratt and Borrego	**LAST UPDATED**	2/22/2025
		ORIGINAL DATE	2/4/2025
SHORT TITLE	PERA Two Percent Cost of Living Adjustments	**BILL NUMBER**	Senate Bill 30/aSHPAC
		ANALYST	Simon

APPROPRIATION*
(dollars in thousands)

FY25	FY26	Recurring or Nonrecurring	Fund Affected
	$10,000.0	Recurring	General Fund

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent analysis of this legislation.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT*
(dollars in thousands)

Agency/Program	FY25	FY26	FY27	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
Cost-of-Living Adjustments for State Members				See Fiscal Implications		PERA Trust Fund

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent analysis of this legislation.
**Cost reported are total costs over the life of the proposed benefit increase

Duplicates House Bill 164; Relates to House Bill 96 and Senate Bill 117

Sources of Information

LFC Files

<u>Agency Analysis Received From</u>
Public Employees Retirement Association (PERA)
Educational Retirement Board (ERB)
New Mexico Municipal League (NMML)

SUMMARY

Synopsis of SHPAC Amendment to Senate Bill 30

The Senate Health and Public Affairs Committee amendment to Senate Bill 30 would limit the annual 2 percent cost-of-living adjustments for retirees over age 65 to apply from FY26 through FY30.

Synopsis of Original Bill

Senate Bill 30 (SB30) would increase annual cost-of-living adjustments for retirees from state government receiving benefits from the Public Employees Retirement Association (PERA) who are 65 or older. Additionally, the bill would allow local governments to opt into a program to have cost-of-living adjustments increased for retirees from their governments by making contributions to cover the actuarial impact of the increased contribution.

SB30 appropriates $10 million from the general fund to PERA to fund cost-of-living adjustment increases for state government retirees.

This bill does not contain an effective date and, as a result, would go into effect 90 days after the Legislature adjourns if enacted, or June 20, 2025. However, the bill's provisions are specific to increase in FY26 and future years.

FISCAL IMPLICATIONS

SB30 would increase benefits paid by PERA for state government employees and could increase benefits paid by PERA for local government employees. Article XX, Section 22, of the New Mexico Constitution prohibits the Legislature from enacting any law that increases the benefits paid by PERA unless adequate funding is provided. That section assigns the PERA board the sole and exclusive power to adopt actuarial assumptions, based on recommendations from an independent actuary.

The bill includes a $10 million appropriation to PERA to provide cost-of-living adjustments to retirees from state government. However, PERA's actuaries estimate a one-time appropriation of $182.4 million is necessary to cover the current and future costs of the bill. Alternatively, if the Legislature provided annual appropriations for the next five years of $41.7 million, PERA's actuaries estimate it would cover current and future costs of the benefits payments. Total costs are higher over five years because PERA's actuaries assume investment income from receiving funds up front would offset costs that would otherwise be paid over a longer period.

Actuarial analysis of the original bill showed relatively modest costs for retirees from state employment in initial years, only $2.6 million for the 11.3 thousand retirees impacted by the legislation, rising to $14.5 million for 12.3 thousand members in FY30. PERA's actuaries projected cost to the PERA funds for only the state general and state police division. Future costs increase both due to an increase in the number of retirees eligible for the benefit (as younger retirees reach age 65) but also due to the compounding of the benefit. Because of the compounding, increased costs will continue even after the sunset included in the amended bill, although growth will be slower before falling as the number of members receiving the additional benefit falls. The full cost of this future growth is included in PERA's cost assumptions, accounting for the large estimate despite lower costs in initial years.

The general fund appropriation included this bill is a recurring expense to the general fund, which are not generally assumed to be time limited. Were the $10 million included in the bill to be provided for a long enough period it could cover the full actuarial cost. PERA estimates total costs of $182.4 million if fully prefunded, versus total costs of $208.5 million if funded over a five year period. Given this, it would likely take significantly more than 20 years of $10 million payments to cover the cost as determined by PERA's actuary. Future appropriations would be dependent on the will of future Legislatures. It is unclear what would happen if a future Legislature chose not to make a future appropriation to the fund, thus rendering the funding inadequate to cover the cost of the benefit increase.

Notably, a direct general fund appropriation diverts from typical practice in funding New Mexico's pension plans. Currently, PERA receives employer and employee contributions automatically as a percent of payroll, based on rates set in statute. This negates the need for regular general fund appropriations and benefits payments are not subject to legislative appropriation. (The Legislature does make appropriations for agency operations.)

Additionally, the bill would allow local governments to participate in the increased benefit, provided the government makes a contribution to PERA to cover the costs. This requirement could allow for adequate funding for these COLAs, assuming the calculations property reflect PERA's actuarial assumptions (see "Technical Issues"). PERA estimates prefunding costs of this benefit to be $177.1 million, assuming all eligible local governments opt in. With funding spread over five years, up to $40.5 million would be needed annually. The bill determines eligibility for an increased COLA based on the division from which a PERA member retires. While increased COLAs for municipal members are contingent on receipt of funding from the local government, increased COLAs for state members are automatic. Analysis from PERA notes a member could receive a higher benefit if retiring from the state, even if the member was only employed by the state for a brief period.

The New Mexico Municipal League (NMML) states the differential treatment between different PERA members is unfair to local government employees and is a departure from the agreed on framework for solvency adopted in 2020 (see "Significant Issues"). Overall, the three municipal plans are better funded than two state government plans, with total assets of $9.9 billion and total liabilities of $14.1 billion, for a funded ratio of 70.3 percent, while the state plans have total assets of $7.9 billion and liabilities of $12.4 billion, for a funded ratio of 63.7 percent. NMML notes, because the state is not covering the full actuarial costs of the increased COLA for state employees, SB30 could result in local government contributions subsidizing increased COLAs for state government employees.

Any unexpended or unencumbered balance remaining at the end of FY27 will not revert to the general fund. Although the bill does not specify funds will revert, presumably unused funds from the appropriation would remain with PERA.

SIGNIFICANT ISSUES

In 2020, the Legislature passed Senate Bill 72 (SB72), which amended the Public Employees Retirement Act to replace an annual 2 percent cost-of-living adjustment (COLA) for most members with new "risk-sharing" COLA, following a temporary suspension of the annual COLA in FY21 through FY23. In those years, the annual COLA was temporarily replaced by an additional, non-compounding payment of 2 percent of the member's benefit. Those additional payments, sometimes called the "13th check," were made for three years and the Legislature appropriated $55 million from the general fund to cover the costs of these payment. Following the three-year period, the new "risk-sharing" COLA was implemented. Unlike the 13th check, this payment would compound. The COLA would be based on the plan's investment performance and the plan's funded status—or the percentage of total liabilities for which the plan has invested assets. Under this COLA, rates would vary from 0.5 percent to 3 percent, until the plan is fully funded, at which point COLAs could go as high as 5 percent.

SB72 was passed to address chronic underfunding issues at PERA. At the time, PERA's actuaries estimated the fund held about 70 percent of the assets needed to pay all accrued benefits, but over time that gap was expected to grow because contributions into the fund were not sufficient to pay all protected benefits, make additional annual cost-of-living adjustments, and pay off the plan's unfunded liability. Actuaries were projecting an infinite funding period, meaning PERA was never expected to hold the assets needed to pay the liabilities. PERA's most recent actuarial valuation report shows the fund holds about 67.2 percent of assets needed, but the funding period has improved to 52 years, although still above the board's target of 25 years. The plans actuaries recommend increasing contributions to the fund, noting contributions needed to meet the funding target would need to rise by an additional 5.37 percent.

SB72 passed at a time when an annual 2 percent COLA was outpacing inflation. Annual COLAs for social security, which are tied to inflation, averaged 1.4 percent between 2010 and 2020. But more recent increases in the cost of living have led these amounts to spike. Social security COLAs in 2022 were nearly 9 percent and were almost 3.2 percent in 2023, which illustrates the challenges faced by retirees in meeting basic needs on fixed incomes.

Exceptions. While most PERA members are subject to the variable COLA, some members continue to receive a fixed 2.5 percent COLA: disability retirees with an annual benefit of less than $25 thousand, normal retirees with 25 years of service credit and a benefit of less than $25 thousand, and retirees who were 75 years old as of July 1, 2020.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Several bills have been introduced to change annual cost-of-living adjustments for PERA members, including:

- House Bill 96 would provide a temporary COLA increase for PERA retirees and appropriates $66 million to fund the increase.
- House Bill 164 is a duplicate of SB30.
- Senate Bill 117 would repeal the current COLA structure and set the annual COLA amount at the amount given for social security.

TECHNICAL ISSUES

Page 6, Lines 10 through 15, allows local governments to opt into the increased COLA, provided the government contribute "in an amount adequate to fund the increase, as determined by the department of finance and administration." This provision may violate Article XX, Section 22, of the New Mexico Constitution, depending on how it is implemented. That section provides:

> A retirement board shall have the sole and exclusive power and authority to adopt actuarial assumptions for its system based upon the recommendations made by an independent actuary with whom it contracts.

Any calculation of an "amount adequate to fund the increase," would necessarily require an actuarial analysis. Were DFA to attempt to determine the amount independent from PERA's contracted actuary, it could be seen to encroach on the retirement system's sole and exclusive power and authority. However, if DFA were to rely on PERA's actuarial calculations and merely communicate those amounts to local governments, this issue could be avoided. However, the sponsor may wish to consider replacing the reference to DFA with "the retirement board," which would avoid a step in the process.

OTHER SUBSTANTIVE ISSUES

SB30 would only apply to public employees who are retired from the Public Employees Retirement Association (PERA). Public employees of school districts and higher education institutions receive benefits from the Educational Retirement Board (ERB). Since 2013, annual cost-of-living adjustments paid by ERB have been limited to improve the fund's solvency. This reform has been partially responsible for improvements to the solvency of that fund. According to ERB's actuary, the plan's funding status is improving, from 60.4 percent in 2020 to 64.8 percent in 2024. The actuaries currently expect the plan to be fully funded in 22 years, significantly less than the amount of time expected for the PERA fund.

Funding additional cost-of-living adjustments for PERA recipients could lead to requests from ERB retirees to receive additional COLAs. In 2020, ERB commissioned a study to examine the differences in benefits between members of ERB and PERA, finding PERA members receive more in pension benefits than ERB-covered employees. This report has resulted in calls for the Legislature to consider "equalizing" pension benefits structures. Funding additional COLAs for PERA members could lead to additional requests from ERB members to supplement that program with general fund appropriations.

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