2011 REGULAR SESSION
ACTUARIAL NOTE HB 530

House Bill 530 HLS 11RS-501 Original **Author: Representative Kevin Pearson** **Date: May 17, 2011** **LLA Note HB 530.01** **Organizations Affected:** **State Retirement Systems** **OR $(369,300,000) APV**	**The Note was prepared by the Actuarial Services Department of the Office of the Legislative Auditor.** Paul T. Richmond Paul T. Richmond, ASA, MAAA, EA Manager Actuarial Services

Bill Header: **RETIREMENT/STATE SYSTEMS:** Relative to state retirement systems, increases employee contributions an average compensation for calculation of benefits.

Cost Summary:

Actuarial Cost/(Savings) to Retirement Systems and OGB	$(369,300,000)
Total Five Year Fiscal Cost	
Expenditures	$(232,400,000)
Revenues	$(232,400,000)

Estimated Actuarial Impact:

The chart below shows the estimated increase/(decrease) in the actuarial value of benefits, if any, attributable to the proposed legislation. Note: it includes the present value cost of fiscal costs associated with benefit changes. It does **not** include present value costs associated with administration or other fiscal concerns.

Actuarial Cost (Savings) to:	**Increase (Decrease) in The Actuarial Present Value**
All Louisiana Public Retirement Systems	$(369,300,000)
Other Post Retirement Benefits	Savings
Total	$(369,300,000)

Estimated Fiscal Impact:

The chart below shows the estimated fiscal impact of the proposed legislation. This represents the effect on cash flows for government entities including the retirement systems and the Office of Group Benefits.

EXPENDITURES	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**5 Year Total**
State General Fund	$ 0	$ (58,100,000)	$ (58,100,000)	$ (58,100,000)	$ (58,100,000)	$ (232,400,000)
Agy Self Generated	0	Decrease	Decrease	Decrease	Decrease	Decrease
Stat Deds/Other	0	0	0	0	0	0
Federal Funds	0	0	0	0	0	0
Local Funds	0	Incl Above	Incl Above	Incl Above	Incl Above	0
Annual Total	$ 0	$ (58,100,000)	$ (58,100,000)	$ (58,100,000)	$ (58,100,000)	$ (232,400,000)

REVENUES	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**5 Year Total**
State General Fund	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Agy Self Generated	Increase	(58,100,000)	(58,100,000)	(58,100,000)	(58,100,000)	(232,400,000)
Stat Deds/Other	0	0	0	0	0	0
Federal Funds	0	0	0	0	0	0
Local Funds	0	0	0	0	0	0
Annual Total	Increase	$ (58,100,000)	$ (58,100,000)	$ (58,100,000)	$ (58,100,000)	$ (232,400,000)

The above table does not reflect additional contributions that will be received by the retirement system for years when the employer contribution rate exceed 23% of pay and additional employee contributions are triggered. See Analysis of Fiscal Costs for more information.

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Bill Information:

Current Law

Louisiana State Employees' Retirement System (LASERS), Teachers' Retirement System of Louisiana (TRSL) and State Police Pension and Retirement System (STPOL) provide various rules for the calculation of final average compensation. These rules vary from one member group to another. The differences in rules generally pertain to the number of months used in the average and in anti-spiking percentages used to control enhancements of pension benefits resulting from artificial increases in pay levels near retirement.

Employee contribution requirements also vary by retirement system and member group.

Subsection B of R.S. 11:450 contains a provision that requires certain members of LASERS employed in hazardous duty occupations to make employee contributions if they continue to work after exiting DROP.

LASERS, TRSL, and STPOL are funded through employer and employee contributions that are applied against the total salary of every participating active member.

Proposed Law

Final Average Compensation

Current and proposed rules pertaining to calculations of final average compensation are compared below:

Comparison of Final Average Compensation Periods and Anti-Spiking Percentages

	Current Law		House Bill 530
LASERS – Rank and File; Bridge Police	For members joining before June 30, 2006:	3 yrs; 25%	1. Final Average Compensation Period will be 5 Years. 2. Anti-Spiking Percentage will be 5%. 3. These rules will apply to all members regardless of when a member joins the retirement system
	For members joining July 1 2006 to December 31, 2011:	5 yrs; 15%	
LASERS – All Other Members Hired Before 1/1/11	For members joining before January 1, 2011:	3 yrs; 25%	
LASERS – Hazardous Duty (Act 1337)	For members joining on or after January 1, 2011:	5 yrs; 15%	
TRSL - Members Employed in Higher Education	For members joining before January 1, 2011:	3 yrs; 10%	
	For members joining on or after January1, 2011:	5 yrs; 15%	
STPOL	For members joining before January 1, 2011:	3 yrs; 25%	
	For members joining on or after January1, 2011:	5 yrs; 15%	

Employee Contributions

Members of LASERS, members of TRSL employed in higher education, and members of STPOL will all be required to make additional contributions during fiscal years in the future when the employer contribution rate equals or exceeds 23% of pay. For LASERS, the 23% of pay threshold pertains to the aggregate employer contribution rate and not to employer contribution rates applicable to the individual sub plans.

In years when the employer contribution rate equals or exceeds 23% of pay, employees will be required to contribute the following amounts in addition to the amounts required under R.S. 11:62.

- 1.5% of an employee's salary up to $50,000, plus
- 3.0% of an employee's salary that exceeds $50,000.

Technical Corrections

Subsection B of R.S. 11:450 contains a provision that requires certain members of LASERS employed in hazardous duty occupations to make employee contributions if they continue to work after exiting DROP. HB 530 removes this provision from the law because it is redundant to language that immediately precedes it.

Employer Contributions

HB 530 adds subparagraph (b) to R.S. 11:102B(1) . This purpose of this subparagraph is to:

1. Increase the total dollar amount of contributions (employee plus employer) that would be received by each retirement system in years when the employer contribution rate equals or exceeds 23% of pay.

2. Use the contribution increase to reduce the unfunded accrued liability associated with the Original Amortization Base for LASERS and TRSL and to reduce the unfunded accrued liability associated with the largest amortization base for STPOL.

3. Determine an employer contribution rate to be applied to the portion of salaries derived from sources other than the state general fund that is greater than an employer contribution rate to be applied to the portion of salaries derived from state general fund sources.

The language of HB 530 pertaining to employer contributions fails to provide clear guidance on how the objectives stated above are to be accomplished. This actuarial note has been prepared by assuming HB 530 will be amended to provide for rules that correspond to the example given below.

1. The Primary employer contribution rate for 2012-13 (P) will be calculated under current rules based on the June 30, 2011 valuation for LASERS. In preparing this rate, it will be assumed that employee contributions, as provided for under R.S. 11:62, will be paid in each future year for all existing employees.

2. The Alternate employer contribution rate for 2012-13 (A) will also be calculated under current rules based on the June 30, 2011 valuation for LASERS. However, for this calculation it will be assumed that employee contributions, as provided under R.S. 11:62 plus the additional employee contribution rates called for under HB 530, will be paid in each future year for all existing employees.

3. Salaries earned by members of LASERS in 2012-13 will be allocated to salaries derived from federal and local sources (NGFS – salaries derived from sources other than the state General Fund) and salaries derived from the state General Fund (GFS).

4. Employer contributions for 2012-13 will be equal to the sum X + Y where X and Y are calculated in the following manner:

   X = The Primary employer contribution rate multiplied by salaries in 2012-13 derived from sources other than the state General Fund (P x NGFS), and

   Y = The Alternate employer contribution rate multiplied by salaries in 2012-13 derived from the state General Fund (A x GFS).

5. A Surplus Amount will be calculated as (P – A) x NGFS where:

   P is the Primary employer contribution rate,

   A is the Alternate employer contribution rate, and

   NGFS are salaries derived from sources other than the state General Fund.

6. The Original Amortization Base for LASERS will be reduced on June 30, 2013 by the Surplus Amount so calculated.

7. This process will be repeated year after year into the future.

Employer contribution requirements for TRSL will be determined in a manner that is slightly different from LASERS because only the contribution rate for higher education employers should be affected. The following example illustrates the procedure for TRSL.

1. The Primary employer contribution rate for 2012-13 (P) will be calculated under current rules based on the June 30, 2011 valuation for TRSL. In preparing this rate, it will be assumed that employee contributions, as provided for under R.S. 11:62, will be paid in each future year for all existing employees.

2. The Alternate employer contribution rate for 2012-13 (A) will also be calculated under current rules based on the June 30, 2011 valuation for TRSL. However, it will be assumed that employee contributions ,as provided under R.S. 11:62 plus the additional employee contribution rates called for under HB 530, will be paid in each future year for all existing employees. This calculation will also be based on the premise that all members of TRSL will contribute the additional contribution.

3. Salaries earned by members of TRSL employed in higher education in 2012-13 will be allocated to salaries derived from federal and local sources (NGFS – salaried derived from sources other than the state General Fund) and salaries derived from the state General Fund (GFS).

4. Employer contribution rate for 2012-13 for K though 12 employers will be the Primary employer contribution rate.

5. Employer contributions for 2012-13 for higher education employers will be calculated as X + Y where X and Y are calculated in the following manner:

   X = The Primary employer contribution rate multiplied by salaries in 2012-13 of TRSL members employed in higher education derived from sources other than the state General Fund (P x NGFS), and

   Y = The Alternate employer contribution rate multiplied by salaries in 2012-13 of TRSL members employed in higher education derived from the state General Fund (A x GFS).

6. A Surplus Amount will be calculated relative to members employed in higher education as (P – A) x NGFS where:

   P is the Primary employer contribution rate,

   A is the Alternate employer contribution rate, and

   NGFS are salaries derived from sources other than the state General Fund.

7. The Original Amortization Base for TRSL will be reduced on June 30, 2013 by the Surplus Amount so calculated.

8. This process will be repeated year after year into the future.

Employer contributions requirements for STPOL will also be calculated in a manner similar to LASERS. The only exception is that surplus contributions for 2012-13 will be used to offset the largest amortization base resulting from an increase in UAL that occurred in any prior year. This process will also be repeated year after year.

Implications of the Proposed Changes

HB 530 will reduce benefits payable to active members of LASERS, active members of TRSL employed in higher education, and active members of STPOL. In addition, employee contribution requirements will increase for years in which the employer contribution rate exceeds 23% of pay.

Under HB 530, active members of LASERS, active members of TRSL employed in higher education, and active members of STPOL will be required to pay additional contributions whenever the employer contribution rate exceeds 23% of pay. These additional contributions will be used to reduce employer contribution requirements on salaries derived from sources associated with the state General Fund. The employer contribution rate applicable to salaries derived from sources other than the General Fund will not change.

For years in which additional employee contributions are mandated under HB 530, a retirement system will receive more in contributions from employers and employees than it would have received otherwise. The surplus is equal to the additionally required employee contributions minus the difference between the Primary and Alternate rates multiplied by salaries derived from sources other than state General Funds.

This surplus will be used to reduce the outstanding balance of the Original Amortization Bases for LASERS and TRSL as of the beginning of the following fiscal year. The reduced OABs will then be re-amortized in accordance with amortization rules currently specified under R.S. 11:102.1 and R.S. 11:102.2 for TRSL and LASERS respectively. The surplus for STPOL will be used to reduce the outstanding balance of the largest amortization base resulting from an increase in UAL occurring in the past.

If HB 530 is enacted, employer contributions will be reduced in years for which the Primary rate equals or exceeds 23%; employee contributions will be increased; a surplus of contributions will develop; the surplus will be used to reduce the outstanding balance of the UAL; and employer contribution requirements in subsequent years will be reduced.

Cost Analysis:

Analysis of Actuarial Costs

Retirement Systems

The benefit reduction portion of HB 530 will reduce actuarial costs associated with LASERS, TRSL, and STPOL. The savings are summarized below:

	LASERS	TRSL	STPOL	Total
Present Value of Future Benefits	$ 302.0 million	$ 44.0 million	$ 23.3 million	$ 369.3 million
Reduction in the UAL	$ 227.5 million	$ 30.3 million	$ 14.9 million	$ 272.7 million
Reduction in Employer Contributions for 2012-13:				
Normal Cost	$ 15.3 million	$ 2.4 million	$ 0.9 million	$ 18.6 million
Amortization Payments	33.0 million	4.4 million	2.1 million	39.5 million
Total	$ 48.3 million	$ 6.8 million	$ 3.0 million	$ 58.1 million

The employee contribution portion of HB 530 is expected to produce about $49 million of additional contributions from employees for years in which the employer contribution rate for all plans exceeds 23%. The table below shows additional employee contributions by retirement system.

Retirement System	Additional Employee Contributions
LASERS	$ 40.6 million
TRSL	7.4 million
STPOL	1.0 million
Total	$ 49.0 million

This estimate is based on projected salaries for LASERS, TRSL, and STPOL for 2011-12.

Whenever an employer contribution rate exceeds 23% of pay and additional employee contributions are required, total contributions (employer and employee) to the retirement system will be greater than what contributions would have been otherwise. These surplus contributions will be used to reduce the UAL and future amortization payments. We estimate the surplus amounts to be the amounts shown below.

Retirement System	Surplus Amount
LASERS	$ 26.8 million
TRSL	4.9 million
STPOL	0.6 million
Total	$ 32.3 million

Other Post Retirement Benefits

HB 530 should produce a reduction in the actuarial cost associated with post-retirement benefits other than pensions. A cost reduction should occur because benefits will be reduced making it likely that at least some members will postpone retirement until they accumulate a pension equal to what they otherwise would have been entitled without HB 530.

Analysis of Fiscal Costs

Charging a higher employer contribution rate for a state employee funded by federal funds than for an employee funded from other sources may result in a federal disallowance as a result of OMB Circular A-87 requirements. The disallowance could potentially be the full difference between the two rates.

If this disallowance is not made, HB 530 will have the following effects on fiscal costs during the five year measurement period.

Expenditures:

1. Expenditures from General Funds and Local Funds will decrease due to lower contribution requirements attributable to the benefit reduction.

2. Expenditures from the retirement systems (Agy Self Generated) will decrease reflecting smaller pensions due to HB 530.

Revenues:

- TRSL revenues (Agy Self Generated) will decrease because employer contribution requirements will decrease due to the benefit reduction.

- TRSL revenues will increase for years in which the employer contribution rate exceeds 23% of pay because additional employee contributions will be triggered and surplus contributions will be created.

The retirement systems report that substantial administrative cost will be incurred in 2011-12 to implement HB 530. Based on information supplied by the retirement systems, we estimate a one-time administrative cost, in the aggregate, ranging from $100,000 to $500,000.

Actuarial Credentials:

Paul T. Richmond is the Manager of Actuarial Services for the Louisiana Legislative Auditor. He is an Enrolled Actuary, a member of the American Academy of Actuaries, a member of the Society of Actuaries and has met the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

Dual Referral:

Senate	**House**
[x] 13.5.1 ≥ $100,000 Annual Fiscal Cost	[ ] 6.8(F)(1) ≥ $500,000 Annual Fiscal Cost
[ ] 13.5.2 ≥ $500,000 Annual Tax or Fee Change	[x] 6.8(F)(2) ≥ $100,000 Annual SGF Fiscal Cost
	[ ] 6.8(G) ≥ $500,000 Annual Tax or Fee Change