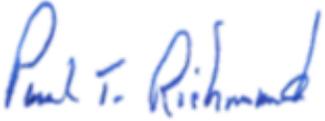


**2012 REGULAR SESSION
ACTUARIAL NOTE SB 52**

<p>Senate Bill 52 SLS 12RS-125 Original</p> <p>Author: Senator Elbert L Guillory Date: April 14, 2012</p> <p>LLA Note SB 52.01</p> <p>Organizations Affected: Louisiana State Employees' Retirement System (LASERS) Teachers' Retirement System of Louisiana (TRSL)</p> <p>OR DECREASE APV</p>	<p>The Note was prepared by the Actuarial Services Department of the Office of the Legislative Auditor.</p> <div style="text-align: center;">  Paul T. Richmond, ASA, MAAA, EA Manager Actuarial Services </div>
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Bill Header: RETIREMENT SYSTEMS: Increases the employee contribution rate for certain members of state retirement systems (7/1/12).

Cost Summary:

Actuarial Cost to Retirement Systems and OGB	Decrease
Total Five Year Fiscal Cost	
Expenditures	Decrease
Revenues	\$0

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.

<u>Actuarial Cost to:</u>	<u>Increase (Decrease) in The Actuarial Present Value</u>
All Louisiana Public Retirement Systems	Decrease
Other Post Retirement Benefits	\$0
Total	Decrease

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	2012-13	2013-14	2014-15	2015-16	2016-17	5 Year Total
State General Fund	Decrease	Decrease	Decrease	Decrease	Decrease	Decrease
Agy Self Generated	Increase	Increase	Increase	Increase	Increase	Increase
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	Decrease	Decrease	Decrease	Decrease	Decrease	Decrease

REVENUES	2012-13	2013-14	2014-15	2015-16	2016-17	5 Year Total
State General Fund	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Agy Self Generated	0	0	0	0	0	0
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	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0

Note: All actuarial and fiscal cost information shown in this actuarial note is based on the assumption that any challenges to the constitutionality of SB 52 will be unsuccessful.

Actuarial Note Highlights

1. Employees will be required to contribute 3% of pay more under SB 52 than they currently contribute.

**2012 REGULAR SESSION
ACTUARIAL NOTE SB 52**

2. Members early in their career will receive less from the retirement plan than what they would have received had they invested their own contributions.
3. Employer contributions to LASERS will be reduced by \$55.7 million a year (2.2% of pay) and employer contributions to TRSL will be reduce by \$10.5 million a year (0.3% of pay).
4. Savings to the state may be delayed due to constitutional challenges.
5. An actuary providing an actuarial valuation for LASERS or TRSL may be required under actuarial standards of practice to either establish a contingency reserve for the potential liability should SB 52 be declared unconstitutional or issue a caveat with his report indicating that all potential liabilities have not been accounted for.

Bill Information:

Current Law

Under current law, active members of the Louisiana State Employees' Retirement System (LASERS) and members of the Teachers' Retirement System of Louisiana (TRSL) contribute various percentages of their salary to the retirement system.

Proposed Law

SB 52 changes employee contribution rates for members of LASERS in the following manner:

Member Category	Current Law	SB 52
Judges, court officers, the governor, the lieutenant governor, and legislators who joined LASERS before January 1, 2011	11.5%	14.5%
Judges who join LASERS on or after January 1, 2011	13.0%	16.0%
Court officers, the governor, the lieutenant governor, and legislators who join LASERS on or after January 1, 2011	8.0%	11.0%
Clerk and sergeant at arms of the House of Representatives and the Secretary and sergeant at arms of the Senate who joined LASERS: Before January 1, 2011 On or after January 1, 2011	9.5% 8.0%	12.5% 11.0%
All other employees, except for Public Safety employees, Wildlife Agents, Bridge Police, and members of the Hazardous Duty Services Plan, who joined LASERS: Before January 1, 2011 On or after January 1, 2011	7.5% 8.0%	10.5% 11.0%
Members of TRSL who are employees of an institution of postsecondary education, the Board of Regents, or a postsecondary education management board unless such members have elected to participate in the Optional Retirement Plan (ORP)	8.0%	11.0%

SB 52 provides remedial language specifying that members of the LASERS ORP will be required to contribute 7.5% of pay.

Under SB 52, the following individuals are exempt from the increases in employee contribution requirements as long as they continue to hold the office to which they have been currently elected:

1. The current governor.
2. The current lieutenant governor.
3. All judges currently in office.

**2012 REGULAR SESSION
ACTUARIAL NOTE SB 52**

4. All current legislators who are members of LASERS.
5. Any other elected official who is a member of LASERS.

SB 52 as amended also will require PRSAC to reconvene to reset the employer contribution rate for 2012-13 to reflect the provisions of the bill.

Implications of the Proposed Changes

All state employees who are members of LASERS and all members of TRSL who are employed in higher education, except those employed in positions that provide for participation in one of the hazardous duty sub plans, current judges, the current governor, the current lieutenant governor, current members of the legislature, and members of TRSL employed in higher education not participating in OPR, will contribute 3.0% more of their pay to LASERS and TRSL than they do currently. These contributions will reduce contribution requirements that would otherwise be paid by the state.

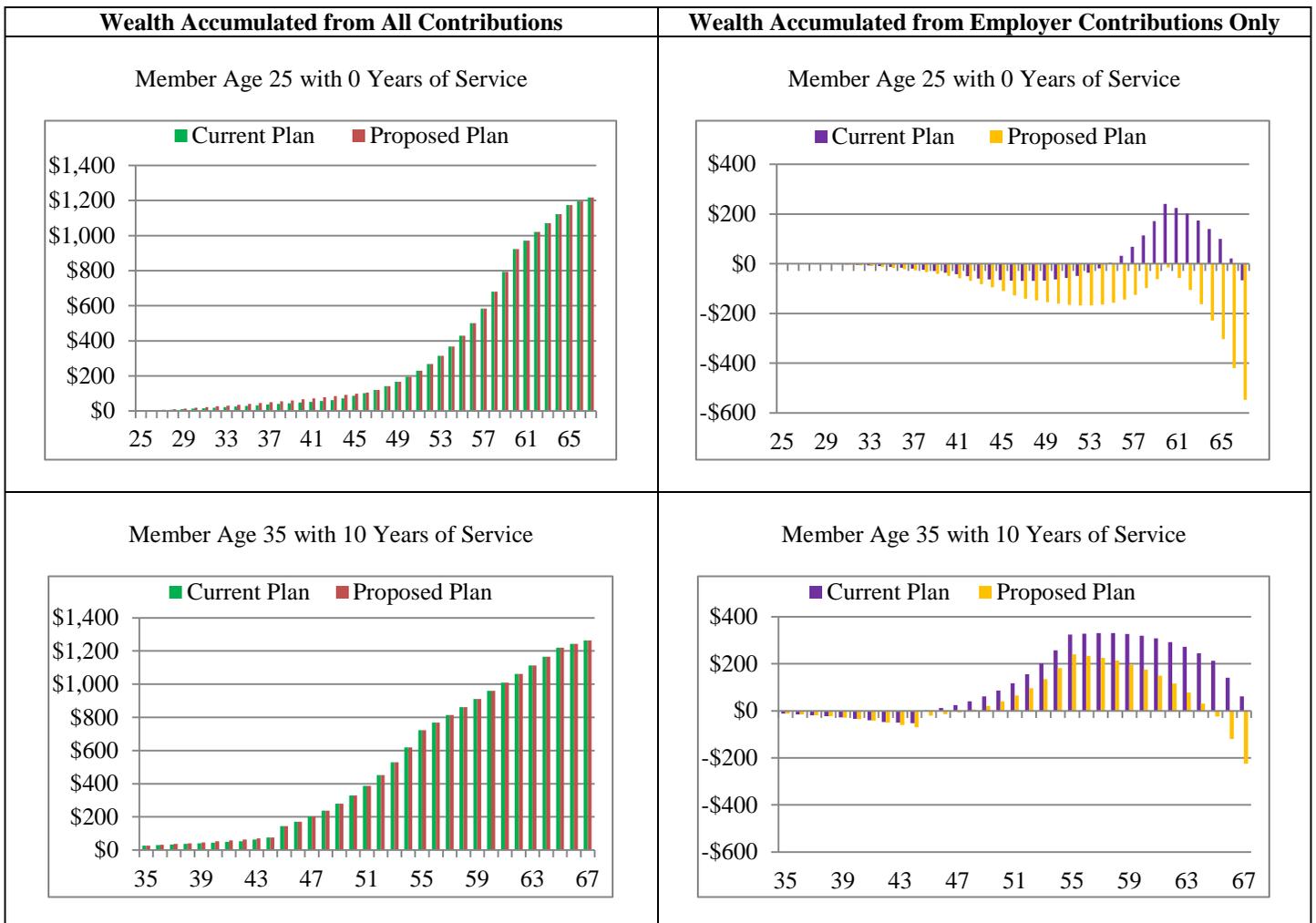
Cost Analysis:

Analysis of Actuarial Costs

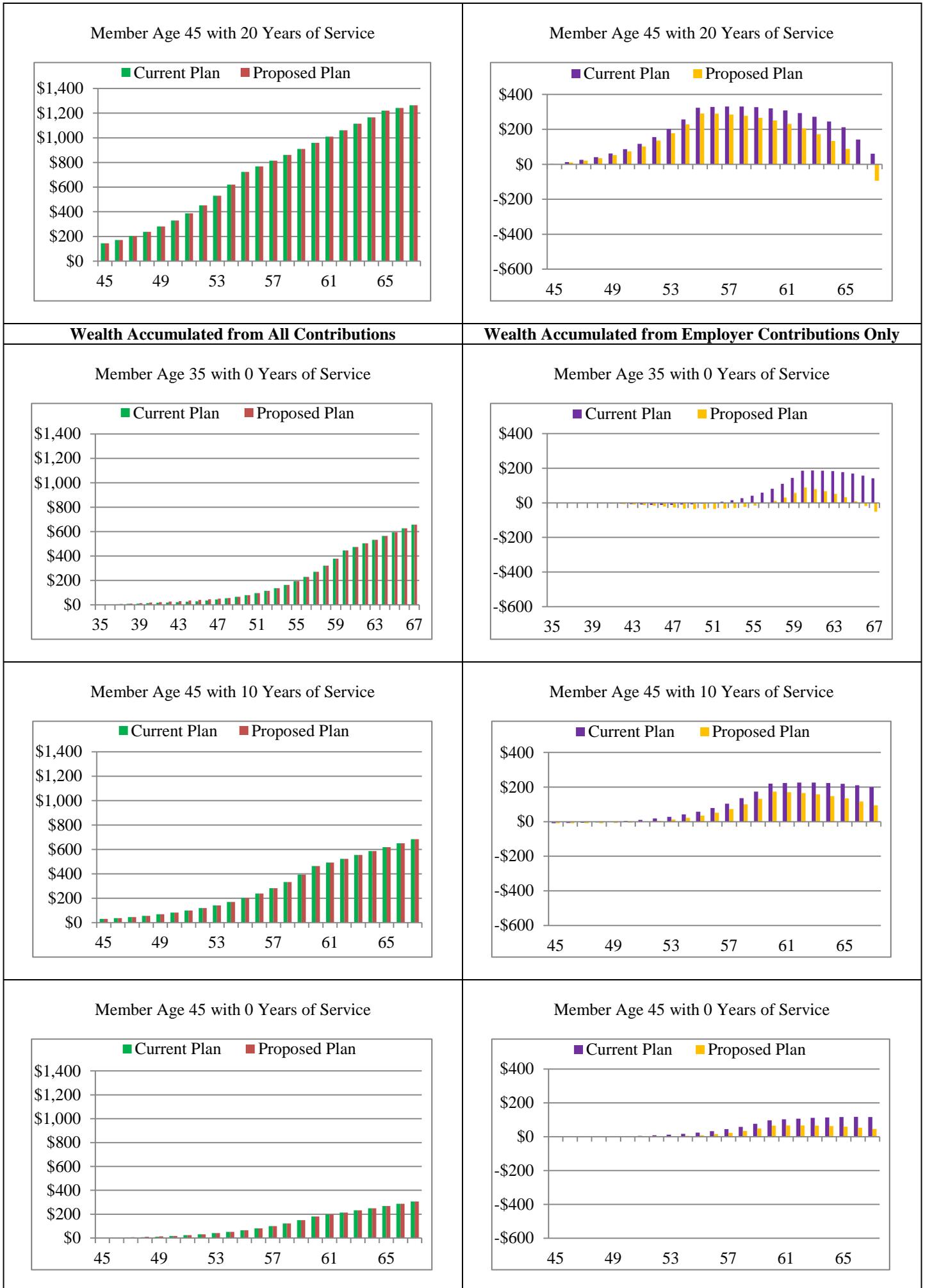
Retirement Systems

Effect of SB 52 on Members

An analysis of the wealth a member will accumulate over his career, with and without enactment of SB 52, is given below for a representative sample of members. Each example is based on a member who is currently earning \$30,000. The total wealth accumulated from employee and employer contributions is shown as well as the wealth accumulated from employer contributions only.



**2012 REGULAR SESSION
ACTUARIAL NOTE SB 52**



Note: A member “earns” negative wealth from the state when the benefit provided by the retirement system has less value than his own contributions accumulated with interest.

The following conclusions can be drawn from these exhibits.

1. The right column of charts demonstrates that SB 52 will have no effect on the total benefit that will be delivered to members.

**2012 REGULAR SESSION
ACTUARIAL NOTE SB 52**

2. The left column shows that benefits attributable to employer contributions will be reduced, in some instances quite substantially.
3. For example, a new employee hired at age 25 may be better off having no pension plan at all. He might be better off retaining his own contributions and investing them himself.
4. An employee currently age 35 with 10 years of service will receive employer provided benefits under SB 52 that are only worth 35% to 50 % as he would receive under current law.
5. An employee currently age 45 with 20 years of service will receive employer provided benefits under SB 52 that are worth about 80% of the benefit he would receive under current law.
6. Similar observation can be made about a new employee hired at age 35 or at age 45.

Effect of SB 52 on Actuarial Costs

SB 52 will have the following effect on the various measures of actuarial cost.

LASERS

	Before Change	After Change	Increase/(Decrease)
Accrued Liability	\$ 15,862,100,000	15,887,500,000	\$ 25,400,000
Total Normal Cost	372,900,000	315,100,000	(57,800,000)
Employer Normal Cost	172,900,000	115,100,000	(57,800,000)
Amortization of Accrued Liability	545,900,000	548,000,000	2,100,000
Employer Contribution Requirements	718,900,000	663,200,000	(55,700,000)
Payroll for Normal Costs	2,549,600,000	2,549,600,000	0
Payroll for Amortization Costs	2,549,600,000	2,549,600,000	0
Employer Normal Cost Rate	6.7827%	4.5167%	(2.2660)%
Employer Amortization Rate	21.4130%	21.4924%	0.0794%
Total Employer Rate	28.2%	26.0%	(2.2)%

TRSL

	Before Change	After Change	Increase/(Decrease)
Accrued Liability	\$ 24,942,200,000	\$ 24,942,900,000	700,000
Total Normal Cost	568,000,000	557,700,000	(10,300,000)
Employer Normal Cost	239,100,000	228,800,000	(10,300,000)
Amortization of Accrued Liability	877,200,000	877,000,000	(200,000)
Employer Contribution Requirements	1,116,300,000	1,105,800,000	(10,500,000)
Payroll for Normal Costs	4,119,000,000	4,119,000,000	0
Payroll for Amortization Costs	4,702,300,000	4,702,300,000	0
Employer Normal Cost Rate	5.8055%	5.5555%	(0.2500)%
Employer Amortization Rate	18.6537%	18.6507%	(0.0030)%
Total Employer Rate	24.5%	24.2%	(0.3)%

Total savings from SB 52 for LASERS and TRSL combined are summarized below:

1. The accrued liability in total will increase \$26.1 million.
2. Employer normal costs will decrease \$68.1 million.
3. Amortization costs will increase \$1.9 million.
4. Employer contribution requirements will decrease \$66.2 million.

Realization of these savings may be delayed or may never occur. It is likely that the constitutionality of SB 52 will be challenged in state or federal courts. According to a memorandum issued by Strasburger, Attorneys at Law to the Office of the Louisiana Legislative Auditor on March 26, 2012, entitled Legal Analysis of 2012 Pension Bills (see www.la.gov/reports_data/actuaryreports) challenges would likely allege violations under:

1. Article X, §29 of the Louisiana Constitution which protects public pension benefits,
2. The Contract Clause within both the Louisiana and U.S. Constitutions claiming contract impairment due to diminished benefits,
3. The Takings Clause of both the Louisiana and U.S. Constitutions for divesting public employee benefits without just compensation,

**2012 REGULAR SESSION
ACTUARIAL NOTE SB 52**

4. The Due Process Clauses of both the Louisiana and U.S. Constitution and the Fifth Amendment to the U.S. Constitution for depriving employees of property rights without due process, and
5. 42 U.S.C. §1983 against public officials for enforcing unconstitutional laws.

The uncertainty regarding the constitutionality of SB 52 poses a dilemma for the retirement systems and the actuaries that provide advice to them. How should they respond to the uncertainty? SB 52 provides that PRSAC shall meet to adopt revised valuations for LASERS and TRSL prepared in accordance with R.S. 11:102, applying the provisions contained in the bill. On the other hand, the Article X, §29(E)(1) makes the following statement about Actuarial Soundness: “The actuarial soundness of state and statewide retirement systems shall be attained and maintained and the legislature shall establish, by law, the particular method of actuarial valuation to be employed for purposes of this Section.”

An actuary employs many actuarial methods in preparing a valuation – the actuarial funding method, the method used to establish the actuarial value of assets, methods for dealing with difficult benefit provisions that are not easily modeled, methods to account for contingent liabilities, etc. The only actuarial method specifically established by the law is the actuarial funding method which for LASERS and TRSL is the Projected Unit Credit Funding Method. The actuary is free to use whatever other techniques, acceptable under Actuarial Standards of Practice, to maintain actuarial soundness in compliance with the Louisiana Constitution.

Implementing the provisions of SB 52, without any recognition of the constitutional challenges, may not be actuarially sound. The actuary may have two choices – prepare the valuation as required by SB 52 with a caveat that the valuation may not maintain the actuarial soundness of the retirement system, or prepare the valuation as required by SB 52 with due allowance for a contingency reserve in the event the law is declared unconstitutional.

Some elements of SB 52 can be reversed should the bill be enacted and the courts later declare it unconstitutional. Employee contributions made in excess of 8.0% as required under current law may be refunded, perhaps with interest. However, such refunds will create a new unfunded accrued liability when such a declaration is made. To avoid this, the retirement systems may elect to establish a contingent liability that would be released only if the constitutionality of SB 52 is upheld. The system actuaries would then prepare their valuations showing the gain relative to the provisions of SB 52, but would also include the contingent liability associated with the constitutionality issue. These amounts would be offsetting and employer contribution requirements would not change until the issue is resolved.

Unless an injunction against implementation is given, the employers will withhold additional contributions from employees and submit them to the retirement systems in accordance with the provisions of SB 52, even though the law is being challenged. However, if the retirement systems do not establish contingent liabilities to keep contribution requirements where they are currently, significant new unfunded accrued liabilities will be incurred if the law is declared unconstitutional. Actuarial recognition of the provisions of SB 52 without the establishment of contingent liabilities might be considered imprudent, against actuarial standards of practice, perhaps against GASB accounting standards, and perhaps against actuarial soundness provisions of the Louisiana constitution.

It is unclear what actions may be taken by the courts, by the retirement systems, or by their actuaries to mitigate damages that might be incurred should SB 52 be overturned. It is therefore also unclear whether or not any actuarial savings to the state will materialize from the bill.

Other Post Retirement Benefits

There are no actuarial costs associated with SB 52 for post-employment benefits other than pensions.

Analysis of Fiscal Costs

The effects of SB 52 on fiscal costs are given below assuming the constitutionality of SB 52 will be upheld should it be challenged.

Expenditures:

1. Expenditures from state General Funds will decrease because employer contribution requirements will decrease by about \$66.2 million a year.
2. Expenditures from the General Fund will increase to the extent that the state will be required to defend the legal challenges that will be brought to the courts. Additional litigation costs that may be incurred by various government entities relative to SB 52 have been estimated to range from \$750,000 to \$3,000,000.
3. Expenditures from LASERS and TRSL (Agy Self-Generated) will increase because affected members who terminate employment will receive larger refunds than what they would have received without SB 52.
4. Expenditures by LASERS and TRSL (Agy Self-Generated) will increase because of implementation costs which are estimated to be about \$26,000 in FY 2013.

Revenues:

1. LASERS and TRSL revenues (Agy Self-Generated) will not change because employee contributions will be substituted for employer contributions.

**2012 REGULAR SESSION
ACTUARIAL NOTE SB 52**

The effect of SB 47 on actuarial and fiscal savings may change from the amounts shown above based on the following:

1. The constitutionality of SB 52 is likely to be litigated.
2. The potential success of such litigation is unknown, but reasonable grounds have been established.
3. It may take several years for the legal challenges to work through the court system.

The outcome of such litigation may take one of the following forms:

1. SB 52 is challenged in the courts and an injunction is given delaying implementation of the provisions of the bill.
2. The retirement systems, the actuaries, or other regulatory bodies believe it necessary to create a contingency reserve to stabilize employer contribution requirements until constitutionality issues relative to SB 52 are resolved.
3. SB 52 is litigated and is declared unconstitutional.
4. SB 52 is litigated and is declared constitutional.

If any outcome except that last occurs, actuarial and fiscal savings may be delayed or may never materialize.

Actuarial Caveat

Actuarial analyses contained in this actuarial note are based on the 8.25% discount rate assumption used by LASERS in the preparation of valuation results as of June 30, 2011 and contribution requirements for FY 2012. Although PRSAC recently adopted a valuation report based on an 8.00% discount rate for estimating contribution requirements for FY 2013, we are continuing to use the 8.25% rate because we started our analysis before the change was approved.

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 necessary to render the actuarial opinion contained herein.

Dual Referral:

Senate

13.5.1 \geq \$100,000 Annual Fiscal Cost

13.5.2 \geq \$500,000 Annual Tax or Fee Change

House

6.8(F) \geq \$500,000 Annual Fiscal Cost

6.8(G) \geq \$500,000 Annual Tax or Fee Change