

2012 REGULAR SESSION  
ACTUARIAL NOTE SB 47

Revised

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| <b>Senate Bill 47 SLS 12RS-129<br/>Reengrossed with Senate Finance<br/>Committee Amendment #3827</b><br><br><b>Author: Senator Elbert L. Guillory<br/>Date: May 9, 2012</b><br><br><b>LLA Note SB 47.03</b><br><br><b>Organizations Affected:</b><br>Louisiana State Employees'<br>Retirement System (LASERS)<br>Teachers' Retirement System of<br>Louisiana (TRSL)<br><br><b>RE DECREASE APV</b> | <b>The Note was prepared by the Actuarial Services Department of the Office of the<br/>Legislative Auditor.</b><br><br><br><b>Paul T. Richmond, ASA, MAAA, EA<br/>Manager Actuarial Services</b> |
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**Bill Header:** RETIREMENT SYSTEMS. Provides relative to final average compensation (6/30/12)

**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.

|                                         |                                                                      |
|-----------------------------------------|----------------------------------------------------------------------|
| <b>Actuarial Cost to:</b>               | <b><u>Increase (Decrease) in<br/>The Actuarial Present Value</u></b> |
| All Louisiana Public Retirement Systems | Decrease                                                             |
| Other Post Retirement Benefits          | Decrease                                                             |
| 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  | 2016-2017 | 5 Year Total |
|--------------------|----------|----------|----------|----------|-----------|--------------|
| State General Fund | Increase | Increase | \$ 0     | \$ 0     | \$ 0      | Increase     |
| 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        | 0        | 0        | 0        | 0         | 0            |
| Annual Total       | Increase | Decrease | Decrease | Decrease | Decrease  | Decrease     |

| REVENUES           | 2012-13 | 2013-14 | 2014-15 | 2015-16 | 2016-2017 | 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 47 will be unsuccessful.

Note: All references to SB 47 in this actuarial note pertain to the Reengrossed version of SB 47 with Senate Finance Committee Amendment #3827.

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Actuarial Note Highlights

- 1. Employees affected by SB 47 will have to work about one more year to replace benefits lost due to the bill’s enactment.
- 2. Employer contribution requirements to LASERS and TRSL will not change as a result of SB 47, because the savings will be used to amortize the UAL more rapidly than currently scheduled.
- 3. Special employer UAL payments will be created for LASERS (about \$25.7 million a year) and for TRSL (about \$2.9 million a year). These payments will be made until the UAL is fully amortized. As a result, the LASERS UAL will be paid off about 6 years ahead of schedule and the final payment in FY 2040 will be reduced for TRSL.
- 4. Savings may be delayed due to constitutional challenges.

Bill Information:

Current Law

Louisiana State Employees’ Retirement System (LASERS) and Teachers’ Retirement System of Louisiana (TRSL) provide various rules for the calculation of final average compensation (FAC). 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.

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                                       | Senate Bill 47                                    |
|--------------------------------------------------------------------|---------------------------------------------------|---------------------------------------------------|
| LASERS – Rank and file members hired on or before July 1, 2006.    | FAC Period: 3 yrs<br>Anti-Spiking Percentage: 25% | FAC Period: 5 yrs<br>Anti-Spiking Percentage: 15% |
| TRSL - Members employed in higher education before January 1, 2011 | FAC Period: 3 yrs<br>Anti-Spiking Percentage: 10% | FAC Period: 5 yrs<br>Anti-Spiking Percentage: 10% |

SB 47 specifically identifies the following members of LASERS as being covered by the new rules pertaining to the calculation of final average compensation and anti-spiking percentages.

- 1. The governor.
- 2. The lieutenant governor.
- 3. Legislators
- 4. House clerk or sergeant-at-arms.
- 5. Senate secretary or sergeant-at-arms.
- 6. State treasurer.
- 7. Judges or court officers first employed on or after January 1, 2011.

Final average compensation and anti-spiking percentages for the following members of LASERS will continue to be 3 years and 25% respectively.

- 1. Judges and court officers first employed before January 1, 2011.
- 2. Members of LASERS employed in hazardous duty positions who were first employed before January 1, 2011.

The new FAC rules will be implemented over a period of three years as follows:

- 1. For members retiring on or before June 30, 2013, the provisions of current law will apply.
- 2. For members retiring on or after July 1, 2013 and on or before June 30, 2015, the averaging period will be 36 months plus the number of whole months since July 1, 2013.

In no event will the final average compensation of an existing member affected by SB 47 be less than what it would have been on June 30, 2013 had he terminated employment on that date.

Other Provisions

SB 47 will apply the savings that result from the benefit provisions of the bill to reduce the unfunded accrued liability. The savings will be determined and applied in the following manner.

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1. The June 30, 2013 actuarial valuations for LASERS and TRSL will be prepared twice. The June 30, 2013 valuation will establish an actual employer contribution rate for FY 2013 without recognition of SB 47 and an actual employer contribution rate for FY 2013 with recognition of SB 47.
2. A special UAL rate will be established that is equal to the difference between the actual employer contribution rates for FY 2013 as measured with and without SB 47.
3. The special UAL rate, which will be paid by the employer, will be charged annually beginning with FY 2014. The charge will be first applied against the Original Amortization Base, next against the Experience Account Amortization Base, and finally against any other bases until the UAL is completely amortized.
4. Payment schedules for all current amortization bases will remain as is and will not be changed because of the more rapid amortization of the UAL.

**Implications of the Proposed Changes**

SB 47 will reduce benefits payable to active rank and file members of LASERS first employed before July 1, 2006 and active members of TRSL employed in higher education who were first employed before January 1, 2011. These employees will have to work for about one additional year in order to replace the benefit lost due to SB 47. Unless the courts find SB 47 to be unconstitutional, these benefit changes will reduce future normal costs, the unfunded accrued liability of the retirement systems, and future employer contributions toward the UAL. However, SB 47 will capture these savings by establishing a special employer UAL rate equal to the difference in employer rates with and without SB 47.

**Cost Analysis:**

**Analysis of Actuarial Costs**

**Retirement Systems**

SB 47 will have the following effect on the various measures of actuarial cost.

**LASERS**

|                                    | <b>Before Change</b> | <b>After Change</b> | <b>Increase/(Decrease)</b> |
|------------------------------------|----------------------|---------------------|----------------------------|
| Accrued Liability                  | \$ 15,862,100,000    | \$ 15,672,800,000   | \$ (189,300,000)           |
| Total Normal Cost                  | 372,900,000          | 364,000,000         | (8,900,000)                |
| Employer Normal Cost               | 172,900,000          | 164,000,000         | (8,900,000)                |
| Amortization of Accrued Liability  | 545,900,000          | 529,300,000         | (16,600,000)               |
| Employer Contribution Requirements | 718,900,000          | 693,300,000         | (25,500,000)               |
| 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%              | 6.4311%             | (0.3516)%                  |
| Employer Amortization Rate         | 21.4130%             | 20.7641%            | (0.6489)%                  |
| Total Employer Rate                | 28.2%                | 27.2%               | (1.0)%                     |

**TRSL**

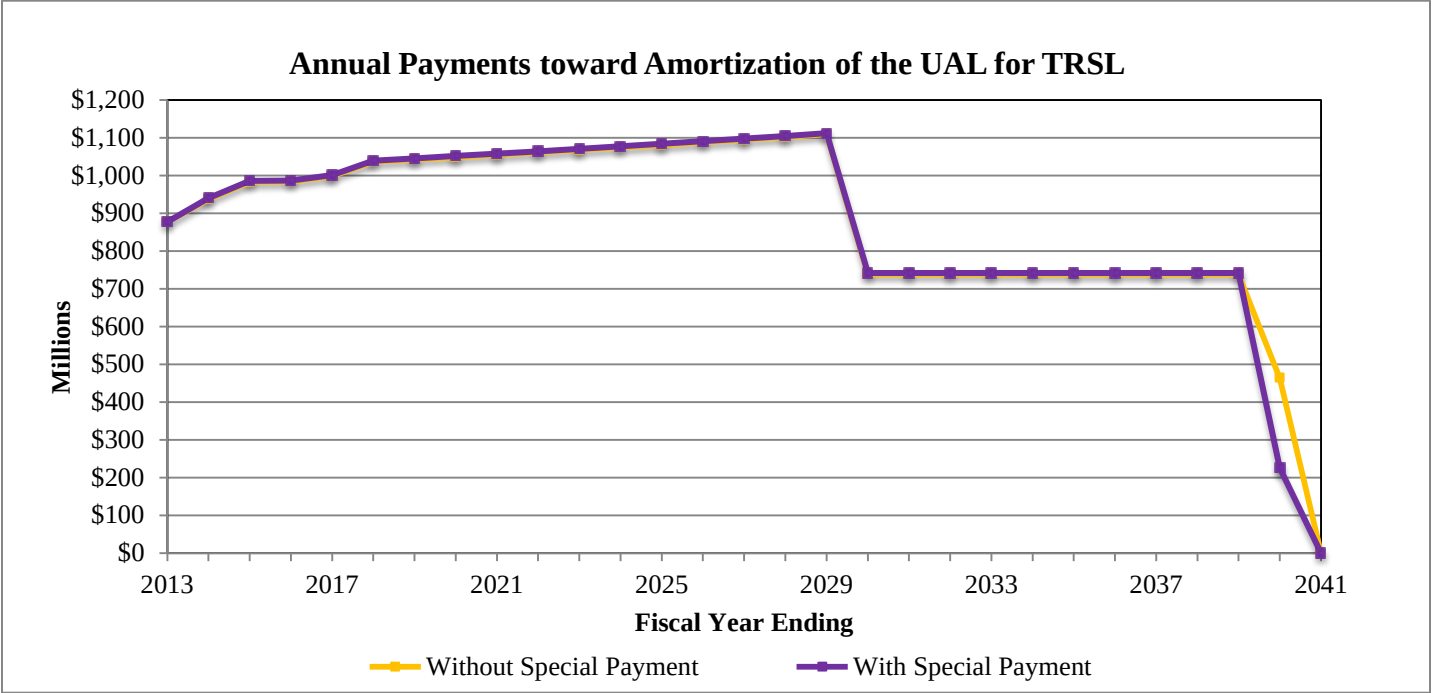
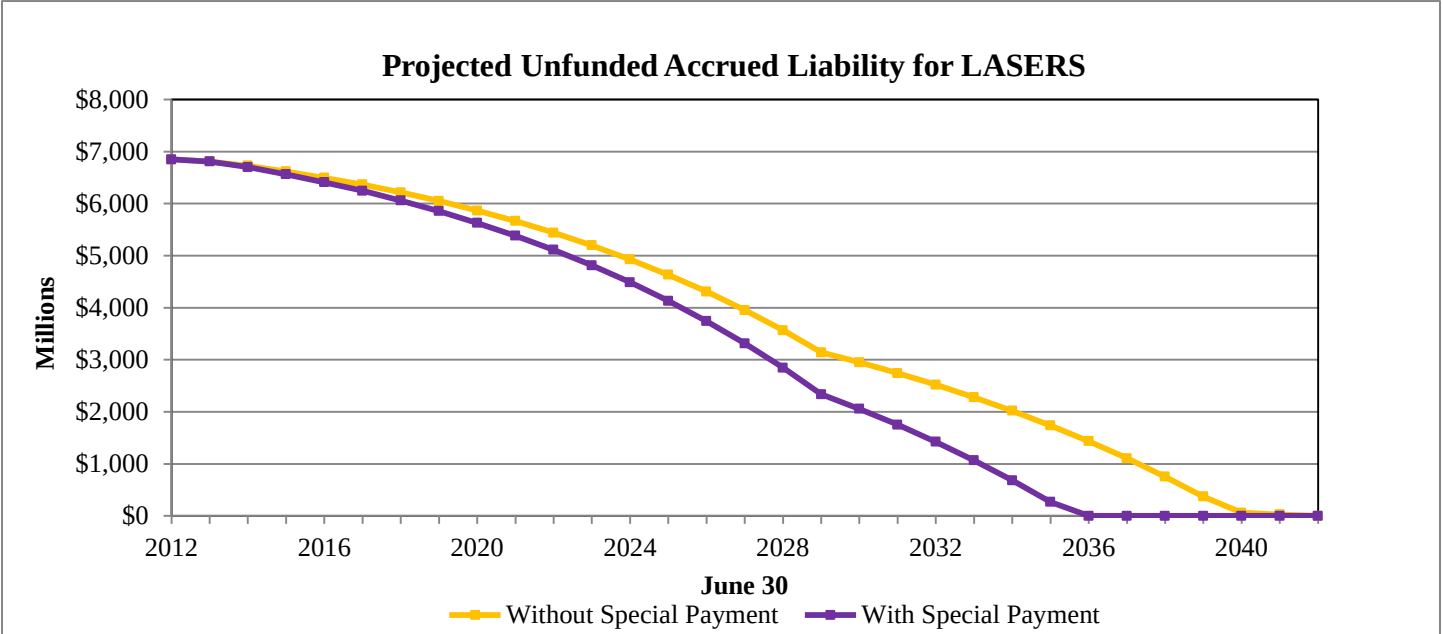
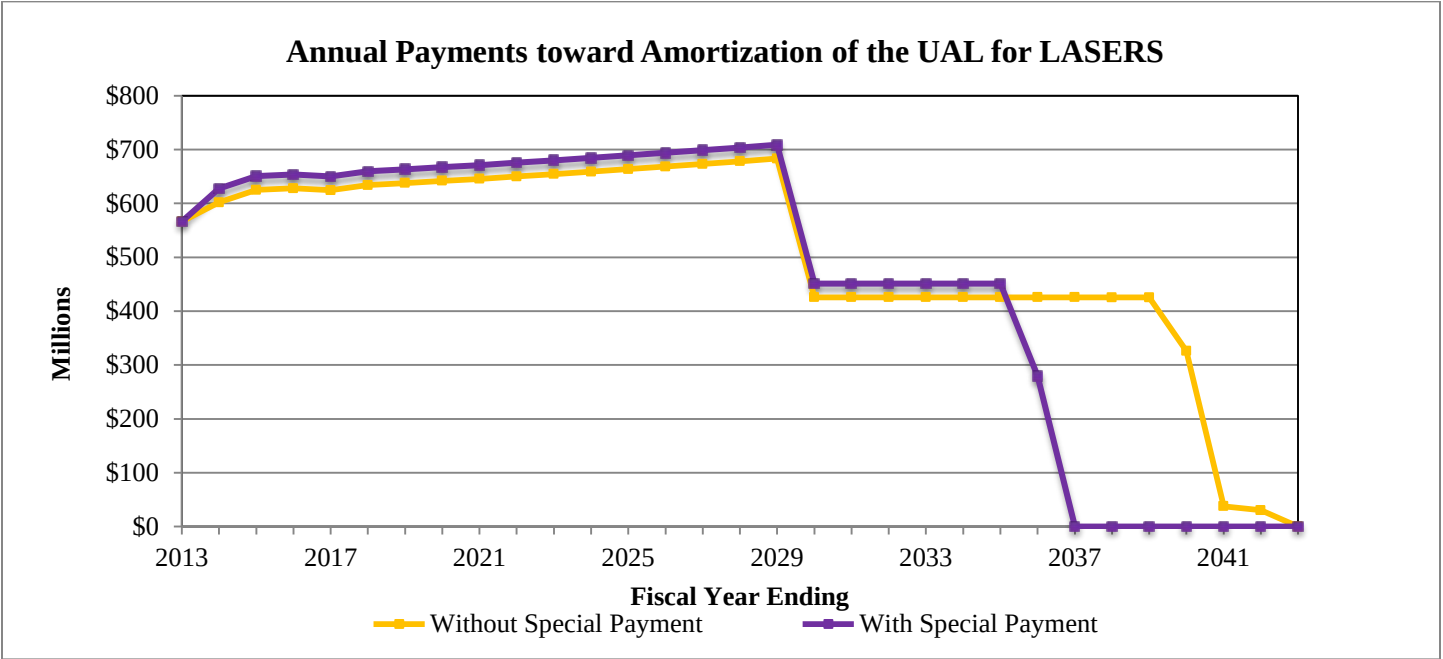
|                                    | <b>Before Change</b> | <b>After Change</b> | <b>Increase/(Decrease)</b> |
|------------------------------------|----------------------|---------------------|----------------------------|
| Accrued Liability                  | 24,942,200,000       | 24,928,700,000      | \$ (13,500,000)            |
| Total Normal Cost                  | 568,000,000          | 566,500,000         | (1,500,000)                |
| Employer Normal Cost               | 239,100,000          | 237,600,000         | (1,500,000)                |
| Amortization of Accrued Liability  | 877,200,000          | 876,000,000         | (1,200,000)                |
| Employer Contribution Requirements | 1,116,300,000        | 1,113,600,000       | (2,700,000)                |
| 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%              | 5.7697%             | (0.0358)%                  |
| Employer Amortization Rate         | 18.6537%             | 18.6287%            | (0.0250)%                  |
| Total Employer Rate                | 24.5%                | 24.4%               | (0.1)%                     |

Total savings from SB 47 for LASERS and TRSL combined are summarized below.

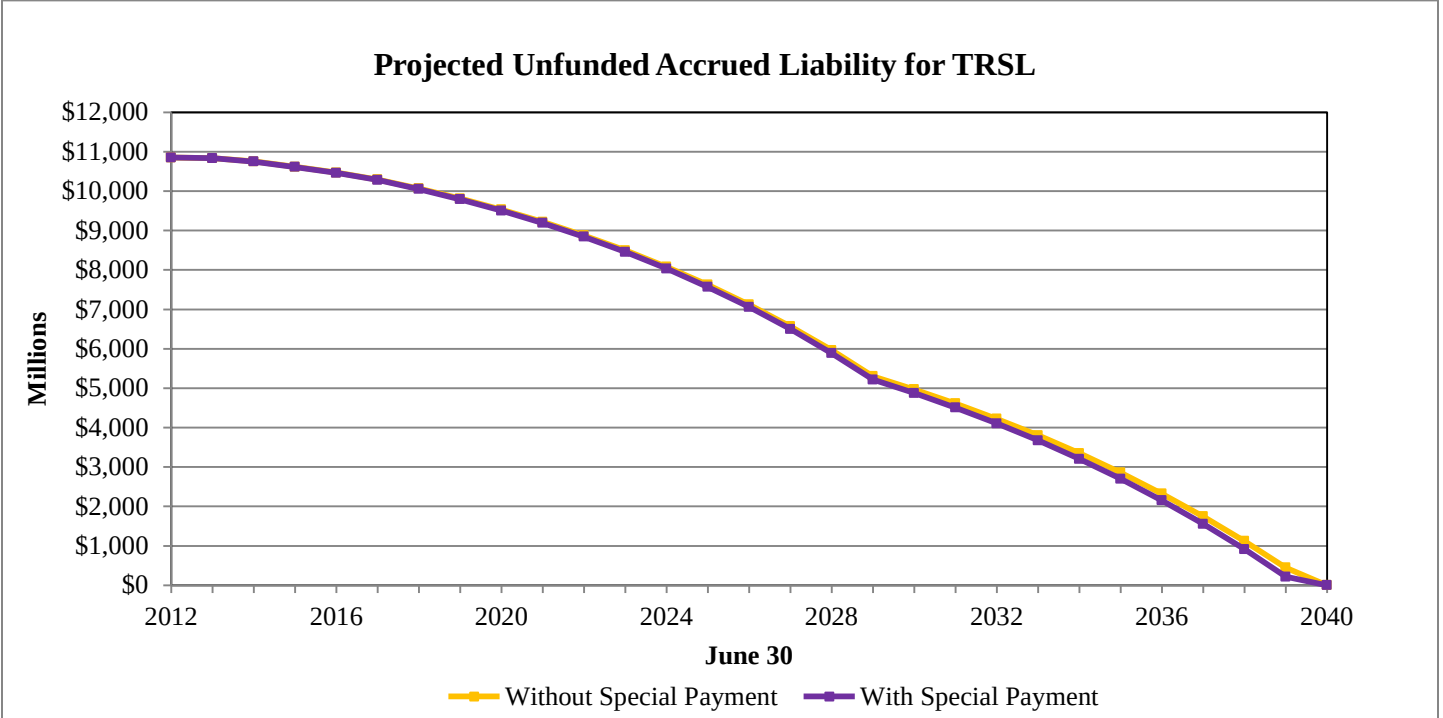
1. The accrued liability in total will decrease \$202.8 million.
2. Employer normal costs will decrease \$10.4 million.
3. Amortization costs will decrease \$17.8 million.
4. Employer contribution requirements will decrease \$28.2million.

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Under SB 47, these savings will be applied to the special employer UAL contribution will be used to reduce the UAL for LASERS and TRSL. As shown in the graphs below, the UAL for LASERS will be fully amortized by June 30, 2037, six years earlier than currently scheduled. For TRSL, full amortization of the UAL will occur in the same year as currently scheduled. However, the final payment will be lower.



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Realization of these savings may be delayed or may never occur. It is likely that the constitutionality of SB 47 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.lla.la.gov/reports\\_data/actuaryreports](http://www.lla.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,
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.

Nevertheless, a determination by the courts on the constitutionality of SB 47 should only have a small impact on actuarial funding for LASERS and TRSL, regardless of the decision. If SB 47 is declared constitutional, nothing changes. If it is declared unconstitutional, then employee benefit rights will be restored. And, because employer contribution requirements have not been reduced, the retirement systems should be able to restore benefit rights, restore UAL balances to their originally scheduled amounts, and resume actuarial funding as if SB 47 had never been enacted.

**Other Post Retirement Benefits**

SB 47 should produce a reduction in the actuarial costs associated with post-retirement benefits other than pensions. A cost reduction should occur because retirement 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 SB 47.

**Analysis of Fiscal Costs**

The effects of SB 47 on fiscal costs are given below assuming the constitutionality of SB 47 will be upheld should it be challenged.

**Expenditures:**

1. Expenditures from state General Funds will not change because employer contribution requirements will remain the same as they would have been had SB 47 not been enacted.
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 47 have been estimated to range from \$750,000 to \$3,000,000.
3. Expenditures from LASERS and TRSL (Agy Self-Generated) will decrease because affected members retiring in the future will receive benefits that are about 5% smaller than they would otherwise receive.
4. Expenditures by LASERS and TRSL (Agy Self-Generated) will increase because of implementation costs which are estimated to be about \$110,000 in FY 2013.

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Revenues:

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

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 47 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 47 is challenged in the courts and an injunction is given delaying implementation of the provisions of the bill.
- 2. SB 47 is litigated and is declared unconstitutional.
- 3. SB 47 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 20, 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 to necessary to render the actuarial opinion contained herein.

**Dual Referral:**

**Senate**

- ☒ 13.5.1 ≥ \$100,000 Annual Fiscal Cost
- ☐ 13.5.2 ≥ \$500,000 Annual Tax or Fee Change

**House**

- ☒ 6.8(F) ≥ \$500,000 Annual Fiscal Cost
- ☐ 6.8(G) ≥ \$500,000 Annual Tax or Fee Change