


**2013 REGULAR SESSION  
ACTUARIAL NOTE HB 61**

<p><b>House Bill 61 HLS 13RS-334 Original</b></p> <p><b>Author: Representative Austin Badon</b></p> <p><b>Date: April 15, 2013</b></p> <p><b>LLA Note HB 61.01</b></p> <p><b>Organizations Affected: State and Statewide Retirement Systems</b></p> <p><b>OR DECREASE APV</b></p>	<p>This Note has been prepared by the Actuarial Services Department of the Office of the Legislative Auditor. The attachment of this Note to HB 61 provides compliance with the requirements of R.S. 24:521.</p> <div style="text-align: center;">   <b>Paul T. Richmond, ASA, MAAA, EA</b>  <b>Manager Actuarial Services</b> </div>
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**Bill Header:** RETIREMENT/STATE-STWIDE: Provides relative to the calculation of benefits for members of state and statewide retirement systems.

**Cost Summary:**

The estimated actuarial and fiscal impact of the proposed legislative is summarized below. Actuarial costs pertain to changes in the *actuarial present value of future benefit payments*. A cost is denoted by "Increase" or a positive number. Savings are denoted by "Decrease" or a negative number.

Actuarial Cost/(Savings) to Retirement Systems and OGB	Decrease
Total Five Year Fiscal Cost	
Expenditures	Decrease
Revenues	Decrease

**Estimated Actuarial Impact:**

The chart below shows the estimated change in the *actuarial present value of future benefit payments*, if any, attributable to the proposed legislation. A cost is denoted by "Increase" or a positive number. Savings are denoted by "Decrease" or a negative number. Present value costs associated with administration or other fiscal concerns are not included in these values.

<b><u>Actuarial Cost/(Savings) to:</u></b>	<b><u>Change in 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. Fiscal costs include estimated administrative costs and costs associated with other fiscal concerns. A fiscal cost is denoted by "Increase" or a positive number. Fiscal savings are denoted by "Decrease" or a negative number.

<b>EXPENDITURES</b>	<b>2013-14</b>	<b>2014-15</b>	<b>2015-16</b>	<b>2016-17</b>	<b>2017-2018</b>	<b>5 Year Total</b>
State General Fund	\$ 0	Decrease	Decrease	Decrease	Decrease	Decrease
Agy Self Generated	Decrease	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	Decrease	Decrease	Decrease	Decrease	Decrease
Annual Total	Decrease	Decrease	Decrease	Decrease	Decrease	Decrease

<b>REVENUES</b>	<b>2013-14</b>	<b>2014-15</b>	<b>2015-16</b>	<b>2016-17</b>	<b>2017-2018</b>	<b>5 Year Total</b>
State General Fund	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
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	\$ 0	Decrease	Decrease	Decrease	Decrease	Decrease

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### **Bill Information:**

#### **Current Law**

Current law establishes the thirteen state and statewide retirement systems and provides various provisions with respect to benefit calculations and the calculation of average compensation.

Current law generally provides for a calculation of benefits for members of the state and statewide retirement systems as follows:

- $\text{Accrual Rate} \times \text{Final Average Compensation} \times \text{Years of Service}$

This benefit calculation is used when a member retires, enters DROP, files for disability benefits, or dies while in active service.

Current law also generally provides for a calculation of final average compensation (FAC) which is the average earnings of a member during a specific period of time. Such calculation of the FAC is typically made over a period of either three or five years, depending on when the member first became eligible for membership in one of the state or statewide retirement systems. The FAC is then used in the calculation of benefits.

#### **Proposed Law**

HB 61 provides for a “divided benefit” for any member of a state or statewide retirement system whose earnings in any given month are 30% or more above his average of monthly earnings for the immediately preceding twelve months. The “divided benefit” calculation is the sum of the following:

1. Total years of service prior to the month in which the 30% or greater increase occurs times the FAC for those particular years of service times the accrual rate for those years of service.
2. Years of service for and after the month in which the 30% or greater increase occurs times the FAC for those particular years of service times the accrual rate for those years of service.
3. A benefit shall also be calculated in a similar manner for any period between two increases of 30% or more.

For a member with a divided benefit, total years of service will be aggregated for purposes of retirement eligibility. HB 61 requires the divided benefit to be used to calculate all benefits earned by the member, including normal retirement benefits, disability benefits, and survivor benefits.

FAC rules under current law are applicable to all periods of service for a member’s divided benefit. For any period of service less than the time period required under current law, the FAC will be the average monthly earnings of the member during the number of months worked for such portion of the divided benefit.

For disability and survivor benefits, HB 61 defines average compensation to mean the sum of all average compensation calculations required under the proposed law with each calculation weighted in proportion to the number of years of service attributable to each calculation and the total number of years of service of the member.

It is assumed that the provisions of HB 61 will be implemented immediately. No phase in of the new FAC provisions will occur.

#### **Implications of the Proposed Changes**

If HB 61 is enacted, a new benefit calculation will be established to further enforce the anti-spiking provisions for members of the state and statewide retirement systems.

### **Cost Analysis:**

#### **Analysis of Actuarial Costs**

##### **Retirement Systems**

If members of state and statewide systems are paid bi-weekly, benefits for retiring members will be based on an average of compensation over an entire career. When paid bi-weekly, an employee receives three paychecks in two months of the year and in some years an employee will receive three paychecks in three months. The pay a member receives in each three paycheck month will exceed the monthly average of pay he receives over the preceding 12 months by more than 30%. As a result, a new divided benefit will be created at least twice a year and in some years three divisions will occur.

If members of state and statewide systems are paid bi-monthly, a divided benefit will occur only when an employee receives a pay increase that exceeds 30%.

In either case, any member of a state or statewide system who is paid 30% more in a month than the average of his pay over the previous 12 months will receive a smaller benefit under HB 61 than he would have otherwise under current law. Therefore, HB 61 will lead to a decrease in the actuarial present value of future benefit payments (APV) and employer contribution requirements.

If members of state and statewide systems are paid bi-weekly, benefits based on FAC amounts are estimated to decrease about 60%. As a result,

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1. The actuarial present value of future benefit payments (APV) is expected to decrease by a significant amount.
2. The accrued liability is expected to decrease by a significant amount.
3. The unfunded actuarial accrued liability is expected to decrease by a significant amount.
4. The normal cost will decrease significantly.
5. Amortization costs will decrease significantly.
6. Ad valorem contributions will decrease significantly.
7. Employer contribution requirements will decrease significantly.

If members of state and statewide systems are paid bi-monthly, benefits will decrease only for individuals who receive a pay raise that exceeds 30%. Benefits for all other members will remain the same. As a result, the actuarial present value of future benefit payments will decrease and employer contribution requirements will decrease. However, the decreases will be small to the point of being negligible.

Realization of these savings may be delayed or may never occur, particularly if members are paid on a bi-weekly basis. It is possible that the constitutionality of HB 61 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](http://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,
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.

**Other Post Retirement Benefits**

If members of the state and statewide systems are paid bi-weekly, members will be more likely to work longer in order to be able to afford to retire. If this occurs, actuarial accrued liabilities for post-employment benefits other than pensions will decrease as a result of HB 61.

If members are paid bi-monthly, HB 61 should not effect when a member decides to retire. Therefore, it is unlikely that HB 61 will have any effect on the actuarial accrued liabilities associated with post-employment benefits other than pensions.

**Analysis of Fiscal Costs**

HB 61 will have the following effects on fiscal costs during the five year measurement period.

Expenditures:

1. Expenditures from the General Fund will decrease beginning in FYE 2015 because employer contribution requirements will be smaller.
2. Expenditures from the state and statewide systems (Agy Self-Generated) will decrease beginning in FYE 2014 because members affected by HB 61 will retire with a smaller benefit than they would have had otherwise.
3. Expenditures from Local Funds will decrease beginning in FYE 2015 because employer contribution requirements will be smaller.

Revenues:

- Revenues to the state and statewide systems (Agy Self-Generated) will decrease beginning in FYE 2015 because employer contribution requirements will be smaller.

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**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