2014 REGULAR SESSION
ACTUARIAL NOTE HB 41

House Bill 41 HLS 14RS-384 Original **Author: Representative J. Kevin Pearson** **Date: March 19, 2014** **LLA Note HB 41.01** **Organizations Affected:** **State Police Retirement System** **OR DECREASE APV**	**This Note has been prepared by the Actuarial Services Department of the Office of the Legislative Auditor. The attachment of this Note to HB 41 provides compliance with the requirements of R.S. 24:521.** Paul T. Richmond **Paul T. Richmond, ASA, MAAA, EA** **Manager Actuarial Services**

<u>Bill Header:</u> RETIREMENT/STATE POLICE: Provides for application of remaining funds in the State Police Retirement System's experience account, after payment of a permanent benefit increase to eligible retirees and beneficiaries, to specified debt of the system.

<u>Cost Summary:</u>

The estimated actuarial and fiscal impact of the proposed legislation 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	$ (4,054,321)
Revenues	$ (4,054,321)

<u>Estimated Actuarial Impact:</u>

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.

Actuarial Cost/(Savings) to:	**Change in the Actuarial Present Value**
All Louisiana Public Retirement Systems	Decrease
Other Post Retirement Benefits	$0
Total	Decrease

This bill complies with the Louisiana Constitution which requires unfunded liabilities created by an improvement in benefits to be amortized over a period not to exceed ten years.

<u>Estimated Fiscal Impact:</u>

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.

EXPENDITURES	**2014-15**	**2015-16**	**2016-17**	**2017-2018**	**2018-2019**	**5 Year Total**
State General Fund	$ 0	Decrease	Decrease	Decrease	Decrease	Decrease
Agy Self Generated	0	Decrease	(114,653)	(1,969,834)	(1,969,834)	(4,054,321)
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	$ (114,653)	$ (1,969,834)	$ (1,969,834)	$ (4,054,321)

REVENUES	**2014-15**	**2015-16**	**2016-17**	**2017-2018**	**2018-2019**	**5 Year Total**
State General Fund	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Agy Self Generated	0	Decrease	(114,653)	(1,969,834)	(1,969,834)	(4,054,321)
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	$ (114,653)	$ (1,969,834)	$ (1,969,834)	$ (4,054,321)

Bill Information:

Current Law

Current law requires a specified portion of investment gains to be transferred from the Regular Benefit Account to the Experience Account. However, current law does not permit a permanent benefit increase (PBI) to be granted without the completion of a significant legislative approval process that includes the introduction of a bill, passage by the House and Senate by a 2/3 vote, and a signature by the governor (see Actuarial Data, Methods, and Assumptions below). If a PBI is granted, an amount equal to the actuarial present value of the PBI is transferred from the Experience Account back to the Regular Benefit Account to offset the additional liability incurred by the system. Any amount in the Experience Account after this transaction remains in the Experience Account for potential later use.

Proposed Law

HB 41 provides that if a PBI is granted in accordance with the PBI formula and eligibility requirements already specified in current law, then any amount in the Experience Account remaining after such PBI grant shall be transferred back to the Regular Benefit Account and used to reduce the balance of the oldest change base. However, the schedule of amortization payments currently associated with the oldest charge base will not be changed.

Implications of the Proposed Changes

Assets remaining in the Experience Account after a PBI is granted will be used to reduce the unfunded accrued liability of the retirement system.

Cost Analysis:

Analysis of Actuarial Costs

Retirement Systems

The PBI formula provides for a 1.5% permanent benefit increase for retirees under age 65 and a 3.5% increase for retirees age 65 and older. If the legislature approves the PBI, then the balance in the Experience Account after the PBI is granted is estimated to be about $13.3 million.

Balance in the Experience Account on July, 1, 2013	$ 18,164,123
Present Value Cost of the Permanent Benefit Increase	4,881,582
Remaining Balance in the Experience Account	$ 13,282,541

HB 41 requires the $13.3 million amount to be transferred back to the Regular Benefit Account and used to reduce the outstanding balance of the charge base originally established on June 30, 1993 (the oldest outstanding positive amortization base). HB 41 also specifies that the amortization payment schedule for this base remain the same as it was before the balance was reduced. As a result, the 1993 charge base will be paid off in 2017 instead of 2029 and interest payments on the debt will be reduced by $23.7 million.

To more completely understand the consequences of the transaction required by HB 41, it is important to know that HB 41 reverses an earlier transaction. A New UAL charge base, or debt, was established for the Regular Benefit Account when the $18.2 million amount was originally transferred to the Experience Account. The New UAL debt was amortized over 30 years with level payments equal to $1.4 million a year. HB 41 returns the $13.3 million to the Regular Benefit Account but instead of reducing the New UAL that had been created, it is used to reduce the charge base established in 1993. A summary of these transactions is given below.

1. The state originally borrowed $18.2 million from the Regular Benefit Account and placed it in the Experience Account. The state, through employer contributions, must pay back the Regular Benefit Account with equal payments over 30 years.

2. HB 41 provides that the residue after funding the permanent benefit increase, $13.3 million, will be transferred back to the Regular Benefit Account.

3. However, the $13.3 million will be applied not to the original debt (the $18.2 million New UAL established June 30, 2013), but rather to the 1993 charge base which is scheduled to be paid off by 2023.

4. The end result is that $13.3 million of the 1993 charge base, which originally was scheduled to be paid off over the next 15 years (by 2029) in accordance with a constitutional mandate, will now be paid off over 30 years.

There is no guarantee that future PBI legislation will follow the eligibility criteria or formulas contained in current law that until now has been subject to a substantively automatic approval process. Nor is there any guarantee, that PBIs in the future will even be based on the balance in the Experience Account. However, as long as the Experience Account is in law, it is likely that the balance in the Experience Account will have some influence on the size of any PBI given. It is also likely that enactment of HB 41 will delay and perhaps limit the size of the next PBI grant given by the legislature.

Therefore, we conclude that the actuarial present value of future benefits will be reduced as a result of HB 41.

Other Post Retirement Benefits

There are no actuarial costs associated with HB 41 for post-employment benefits other than pensions.

Analysis of Fiscal Costs

HB 41 will have the following effects on fiscal costs during the five year measurement period.

Expenditures:

1. Expenditures from the General Fund will decrease because the balance in the Experience Account has been reduced.

2. Expenditures from General Funds will decrease beginning in FYE 2017 because the 1993 charge base will be fully amortized.

3. Expenditures from STPOL (Agy Self-Generated) will decrease because the balance in the Experience Account has been reduced.

Revenues:

1. STPOL revenues (Agy Self-Generated) will decrease because the balance in the Experience Account has been reduced.

2. STPOL revenues will decrease beginning in FYE 2017 because the 1993 charge bases has been eliminated.

Actuarial Data, Methods, and Assumptions

This actuarial note was prepared using actuarial data, methods, and assumptions as disclosed in the most recent actuarial valuation report approved by PRSAC. The actuary signing this note may or may not agree with or endorse these assumptions. He is using this data, methods and assumptions to provide consistency with the actuary for the retirement systems who may also be providing testimony to the Senate and House retirement committees.

Article (10)(29)(F) of the Louisiana Constitution was amended by the legislature and the voters in 2010. This provision states *"Benefit provisions for members of any public retirement system, plan, or fund that is subject to legislative authority shall be altered only by legislative enactment. No such benefit provisions having an actuarial cost shall be enacted unless approved by two-thirds of the elected members of each house of the legislature."* Based on our reading of the amendment, our discussions with General Council for the LLA, and our discussions with legislative staff, we have concluded for the purposes of this actuarial note, that future transfers of investment gains to the Experience Account will occur until the balance in the Experience Account is equal to the cost of a 6% benefit increase for eligible retirees. However, because future COLA grants will require the introduction of a bill, approval by two-thirds of the House and Senate, and the signature of the governor, we assume that COLA grants are ad hoc, and are not automatic

Actuarial Caveat

There is nothing in this bill that has or will compromise the signing actuary's ability to present an unbiased statement of actuarial opinion.

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	House
☐ 13.5.1: Annual Fiscal Cost ≥ $100,000	☐ 6.8(F)(1): Annual Fiscal Cost ≥ $100,000
☐ 13.5.2: Annual Tax or Fee Change ≥ $500,000	☐ 6.8(F)(2): Annual State Revenue Reduction ≥ $500,000
	☐ 6.8(G): Annual Tax or Fee Change ≥ $500,000