2015 REGULAR SESSION
ACTUARIAL NOTE HB 42

House Bill 42 HLS 15RS-172 **Reengrossed 1 with Senate Retirement Committee Amendment #2803** **Author: Representative Sam Jones** **Date: June 3, 2015** **LLA Note HB 42.04** **Organizations Affected:** **State Retirement Systems** **RE1 INCREASE APV**	**The Note was prepared by the Actuarial Services Department of the Office of the Legislative Auditor. The attachment of the Note to HB 42 provides compliance with the requirements of R.S. 24:521.** Paul T. Richmond **Paul T. Richmond, ASA, MAAA, EA** **Manager Actuarial Services**

Bill Header: RETIREMENT/COLAS: Authorizes payments funded by state retirement system experience accounts to certain retirees and beneficiaries of such systems

Cost Summary:

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	Increase
Total Five Year Fiscal Cost	
Expenditures	See Analysis
Revenues	See Analysis

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.

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

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.

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.

EXPENDITURES	**2015-16**	**2016-17**	**2017-18**	**2018-2019**	**2019-2020**	**5 Year Total**
State General Fund	$ 0	$ 0	See Analysis	See Analysis	See Analysis	See Analysis
Agy Self Generated	Increase	See Analysis	See Analysis	See Analysis	See Analysis	See Analysis
Stat Deds/Other	0	0	0	0	0	0
Federal Funds	0	0	0	0	0	0
Local Funds	0	0	See Analysis	See Analysis	See Analysis	See Analysis
Annual Total	Increase	See Analysis	See Analysis	See Analysis	See Analysis	See Analysis

REVENUES	**2015-16**	**2016-17**	**2017-18**	**2018-2019**	**2019-2020**	**5 Year Total**
State General Fund	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Agy Self Generated	0	0	See Analysis	See Analysis	See Analysis	See Analysis
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	See Analysis	See Analysis	See Analysis	See Analysis

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<u>Bill Information:</u>

Comparison of HB 42 with Current Law

Current law provides a template set of provisions setting forth the conditions under which the boards of trustees for the Louisiana State Employees Retirement System (LASERS), the Teachers' Retirement System of Louisiana (TRSL), the Louisiana School Employees' Retirement System (LSERS), and the Louisiana State Police Retirement System (STPOL) can grant a permanent benefit increase (PBI) or cost-of-living-adjustment (COLA). Templates for each system are nearly identical to one another.

Table 1
Comparison of HB 42 with Current Law

	Current Law	**HB 42**
1.	Current law prohibits any system from granting a PBI that becomes effective July 1, 2015	HB 42 allows the state systems to grant a PBI effective July 1, 2015. The amount that may be granted will be determined based on current law, but provisions of current law prohibiting a PBI for July 1, 2015 will be ignored. STPOL will be able to grant the 2.0% special PBI for retirees, beneficiaries and survivors who are age 65 and older.
2.	Investment gains for FYE 2015 that exceed the hurdles imposed under current law may be deposited into the Experience Account on July 1, 2015.	The Experience Account for each system will not receive any credits on June 30 or July 1, 2015. a. The July 1, 2014 balance in the Experience Account will be debited if the return on the actuarial value of assets is negative for FYE 2015. b. No investment credits will be granted if the actuarial return on the actuarial value of assets is positive. c. No investment gains will be transferred from the regular benefit pool of assets to the Experience Account on June 30 or July 1, 2015.
3.	New gains or losses will be amortized with level payments over a 30-year period. Once a system becomes 85% funded, new gains or losses will be amortized with level payments over a 20-year period.	New gains or losses will be amortized with level payments in accordance with the schedule shown below: a. For gains or losses in FYE 2015 – 28 year amortization b. For gains or losses in FYE 2016 – 26 year amortization c. For gains or losses in FYE 2017 – 24 year amortization d. For gains or losses in FYE 2018 – 22 year amortization e. For gains or losses in FYE 2019 – 20 year amortization f. For gains or losses in FYE 2020 or later – 20 year amortization
4.	For LASERS and TRSL • When either the OAB or EAAB are fully liquidated, investment gains that otherwise would have applied to the OAB or EAAB will next be applied to the remaining OAB or EAAB. Gains that remain after the OAB and EAAB have been fully liquidated will then be allocated to the next oldest charge base. The amortization schedule for each such base will not be re-amortized unless the system is 85% funded. For LSERS and STPOL • The same rules apply as for LASERS and TRSL except that gains will initially be allocated to the oldest charge base. LSERS and STPOL do not have either an OAB or EAAB.	Rules under current law continue to apply with the following exceptions applicable to all systems: a. The outstanding balance of the OAB and EAAB for LASERS and TRSL on June 30, 2015 will be re-amortized. The amortization period will not be changed. Amortization payments will increase in accordance with the rules established by Act 497 of the 2009 session. b. For the next 4 valuations, no re-amortization will occur for any bases being reduced by investment gains. c. Re-amortization will next occur with the June 30, 2019 valuation. Re-amortization will then occur every 5th year thereafter. d. This five year process will continue until the system's UAL is $0.
5.	A charge base will be established whenever an amount is transferred to the Experience Account. The base will be amortized with level payments over a 30 year period. Beginning with the June 30, 2019 valuation, new charge bases will be amortized over a 10 year period.	A charge base will be established whenever an amount is transferred to the Experience Account. Beginning with the June 30, 2016 valuation, any new base will be amortized with level payments over a 10 year period.

Implications of the Proposed Changes

In general, HB 42 will accomplish the following:

1. PBIs that might have otherwise been granted effective July 1, 2016 will instead be granted effective July 1, 2015. This guarantees that most of the funds currently in the Experience Account will be used to provide PBIs and will not be available for other purposes.

2. The PBI skip year that otherwise would have occurred beginning July 1, 2015 will now occur beginning July 1, 2016.

3. HB 42 moves Louisiana law closer to the requirements of Actuarial Standards of Practice. The actuaries performing valuations for the state systems will be reporting fewer exceptions to actuarial standards and the actuarial integrity of the retirement systems will increase.

4. The effect of HB 42 on employer contribution requirements will first occur for FYE 2018. The impact may be an increase or a decrease depending upon future events. Some provisions of HB 42 will lead to an increase in contributions; others will lead to a decrease.

Cost Analysis:

Analysis of Actuarial Costs

HB 42 contains benefit provisions having an actuarial cost. As a general rule, retirees will receive PBIs every other year under current law and under HB 42. However, future PBIs will be granted one year earlier under HB 42 than under current law. There is an actuarial cost associated with this change of benefit provisions. However, a reliable estimate of this cost cannot be determined within the time available to prepare this actuarial note.

Retirement Systems

PBIs for 2015 and 2016

The provisions of HB 42 that pertain to PBI grants (Table 1, Items 1 and 2) are the only provisions of HB 42 that result in an actuarial cost. The other provisions of HB 42 (Table 1, Items 3, 4, and 5) neither increase nor decrease actuarial costs, but rather effect the timing and amounts of employer contributions to the retirement system.

HB 42 essentially creates a swap of PBI grants. Under current law, no grants can be made effective July 1, 2015, but it is likely that a full grant could be made effective July 1, 2016. HB 42 reverses the order. A grant will be given effective July 1, 2015, but none will be given July 1, 2016. Additional actuarial costs incurred by the 2015 grant under HB 42 will be offset by actuarial savings associated with the prohibition of grants for 2016.

The actuarial present value cost of the PBI grants is shown in Table 2. These costs are based on the following:

1. LASERS and TRSL will grant a PBI not to exceed 1.5%.

2. LSERS will grant a PBI not to exceed 2.0%.

3. STPOL will grant a PBI not to exceed 2.0%. In addition, STPOL will grant a special 2.0% PBI to retirees who are at least age 65. The special PBI is in addition to the regular PBI.

Table 2
PBIs Effective July 1, 2015 for the State Retirement Systems under HB 42

	LASERS	TRSL	LSERS	STPOL	Total
Number Eligible for a PBI					
Estimated Eligible Regular Retirees	32,472	57,216	10,146	672	100,506
Estimated Eligible Survivors	5,751	6,541	1,662	295	14,249
Estimate Eligible Disabled Retirees	2,506	4,089	331	61	6,987
Total	40,729	67,846	12,139	1,028	121,742
Actuarial Present Value of PBI					
Benefits Increase − Regular Retirees	$ 101,164,238	$ 193,159,879	$ 20,433,791	$ 6,789,714	$ 321,547,622
Benefits Increase − Survivors	10,211,614	13,972,223	2,146,116	1,498,949	27,828,902
Benefits Increase − Disabled Retirees	4,228,693	5,961,764	437,433	361,416	10,989,306
Total	$ 115,604,545	$ 213,093,866	$ 23,017,340	$ 8,650,079	$ 360,098,395
Balance in the Experience Account					
Balance on June 30, 2014	$ 117,093,356	$ 218,148,161	$ 20,787,326	$ 12,069,552	$ 368,098,395

Based on information currently available, PBI grants by LASERS and TRSL could be less than 1.5%. The LSERS PBI grant is very likely to be less than 2.0%. The STPOL PBI grant is likely to be the full 2.0% regular PBI plus the special 2.0% PBI for those who are age 65 and older.

PBIs for 2017 and Later Years

PBI grants for 2017 and later years will be made on average one year sooner under HB 42 than under current law. There is an actuarial cost associated with earlier benefit payments. However, a reliable estimate of this cost cannot be determined given the time available to prepare this actuarial note.

Other Post Retirement Benefits

There are no actuarial costs associated with HB 42 for post-employment benefits other than pensions.

Analysis of Fiscal Costs

1. Analysis of PBI provisions

Each of the four state systems achieved significant investment gains for FYE 2014. As a result, a portion of those gains were transferred from the regular pool of assets to the Experience Account and a new charge base was established on June 30, 2014, equal to the amount so transferred. Employer amortization costs for the next 30 years are now larger than they would have been otherwise. Allocations to the Experience Accounts and 30-year amortization of those allocations are shown below.

Table 3
Experience Account Allocations on June 30, 2014 and Additional Amortization Costs Incurred

	LASERS	TRSL	LSERS	STPOL	Total
Allocations to the Experience Account for FYE 2014	$ 4,590,124	$ 170,334,888	$ 20,787,326	$ 16,675,834	$ 212,388,172
New Amortization Costs for the Next 30 Years until FYE 2043	383,565	14,733,703	1,658,377	1,229,144	18,004,789

However, please note the following:

a. Employers still have 29 years of amortization payments left in order to restore the regular benefit pool of assets to its original position. The Experience Account is funded only because plan sponsors "borrowed" from the regular benefit pool of assets to fund the Experience Account.

b. The average duration of the PBIs to be granted on July 1, 2015, is about 15.5 years. However, employers will be paying for these grants for the next 29 years.

c. Because a charge base was established effective June 30, 2014 to reflect the cost of the anticipated PBI grant to be made either July 1, 2015 or July 1, 2016, a new charge base will not be needed when the PBI grant is actually made.

d. The 2015/2016 PBI swap provisions of HB 42 will have minimum effect on fiscal costs during the five year measurement period.

The retirement systems will begin to make PBI payments for FYE 2016 under HB 42. Under current law, PBI payment would not have begun until 2017. The estimated benefit payment stream for the first five years following a PBI grant is given below.

Table 4
Expenditures Associated with a Single PBI Grant

Year	Increase in LASERS Expenditures	Increase in TRSL Expenditures	Increase in LSERS Expenditures	Increase in STPOL Expenditures	Total Increase in Expenditures
1	$ 11,557,915	$ 22,259,748	$ 2,581,222	$ 833,398	$ 37,232,283
2	11,398,106	21,933,364	2,506,602	811,833	36,649,915
3	11,230,352	21,531,398	2,430,206	789,513	35,981,469
4	11,044,832	21,137,415	2,352,234	766,051	33,300,532
5	10,855,240	20,719,923	2,272,859	741,818	34,589,840
Total	$ 56,086,444	$ 107,581,849	$ 12,143,124	$ 3,942,612	$ 179,754,029

A new benefit stream will be added every other year under current law and under HB 42. The effect on expenditures payable by the retirement systems is compared in Table 5.

Table 5
Benefit Expenditures

Fiscal Year	Current Law	HB 42	Increase/(Decrease)
2015-16	0	37,232,000	37,232,000
2016-17	37,232,000	36,650,000	(582,000)
2017-18	36,650,000	73,213,000	36,563,000
2018-19	73,213,000	69,950,000	(3,263,000)
2019-20	69,950,000	107,803,000	37,853,000
Total	217,045,000	324,848,000	107,803,000

The provisions of HB 42 leading to earlier payment of PBIs beginning in 2017 will eventually require higher employer contribution requirements. The timing and the size of such an increase cannot be determined because the actuarial present value cost of the PBI program is not regularly measured as part of the annual valuation process for each retirement system.

2. Analysis of Reduced Periods for Amortizing Gains and Losses

Periods over which actuarial gains and losses will be amortized are being reduced from 30 years to 20 years. This reduction will be phased in over the next five years. These provisions of HB 42 will effect employer contribution requirements beginning with FYE 2018.

This change in the amortization period may result in larger or smaller employer contribution requirements. If assumptions used to prepare the valuations are correct, then gains will occur in some years and losses in others. These gains and losses will offset one another and in the long run the stream of employer contributions with or without HB 42 will be similar.

However, if actuarial losses exceed actuarial gains, then systematic increases in employer contribution requirements will occur and these increases will be larger than they would have been without HB 42.

3. Re-amortization of the OAB and EAAB

Employer contribution requirements will be reduced as a result of these provisions of HB 42. Currently, investment gains are used to pay off the outstanding balance of the OAB and EAAB sooner than otherwise provided for. Re-amortization under HB 42 will restore the original amortization period, but will reduce amortization payments.

The effect of HB 42 relative to these provisions cannot be measured because they depend on the occurrence of future investment gains. This provision of HB 42 will begin to affect employer contribution requirements in FYE 2018

4. Ten-Year Amortization of Experience Account Transfers

Currently, losses due to transfers from the regular pool of assets to the Experience Account are amortized over 30 years. The amortization period for transfers based on the June 30, 2019 and later valuations will be 10 years. Under HB 42, ten year amortization of transfers will begin with the June 30, 2016 valuation.

This provision of HB 42 will lead to an increase in employer contribution requirements if a transfer occurs between now and June 30, 2019. The first employer contribution that potentially could be affected by this change is the requirement for FYE 2019.

5. The net effect of all provisions of HB 42 on fiscal costs over the five year measurement period are summarized below:

Expenditures:

1. Expenditures from the General Fund in the form of larger employer contribution requirements may increase or decrease.

2. Expenditures from retirement systems (Agy Self Generated) in the form of larger benefit payments will increase for FYE 2016. Expenditures for FYE 2017 and later years may increase or decrease.

3. Expenditures from Local Funds in the form of larger employer contribution requirements may increase or decrease.

Revenues:

- Revenues of the retirement systems (Agy Self-Generated) in the form of larger employer contribution requirements may increase or decrease.

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.

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Actuarial Caveat

There is nothing in HB 42 that will compromise the signing actuary's ability to present an unbiased statement of actuarial opinion.

Actuarial Credentials:

Paul T. Richmond is the actuary 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

- [x] 13.5.1: Annual Fiscal Cost ≥ $100,000
- [ ] 13.5.2: Annual Tax or Fee Change ≥ $500,000

House

- [ ] 6.8(F)(1): Annual State Fiscal Cost ≥ $100,000
- [ ] 6.8(F)(2): Annual State Revenue Reduction ≥ $500,000
- [ ] 6.8(G): Annual Tax or Fee Change ≥ $500,000