


Colorado Legislative Council Staff
STATE, LOCAL, and
STATUTORY PUBLIC ENTITY
FISCAL IMPACT

Drafting Number: LLS 06-0821
Prime Sponsor(s): Sen. Sandoval
 Rep. Marshall

Date: April 24, 2006
Bill Status: Senate SVMA
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TITLE: CONCERNING THE NONCONTRACTUAL PENSION BENEFITS OF PUBLIC EMPLOYEES, AND, IN CONNECTION THEREWITH, MODIFYING, FOR PURPOSES OF THE PUBLIC EMPLOYEES' RETIREMENT ASSOCIATION, THE CURRENT DEFINITION OF SALARY, THE HIGHEST AVERAGE SALARY CALCULATION, THE HEALTH CARE SUBSIDY, AND THE MEMBER AND EMPLOYER CONTRIBUTION PROCESS.

Fiscal Impact Summary	FY 2006/07	FY 2007/08	FY 2008/09
State Revenues			
State Expenditures			
Total		\$1,170,364	\$9,070,781
FTE Position Change	0.0 FTE	0.0 FTE	0.0 FTE
Effective Date: Upon signature of the Governor			
Appropriation Summary for FY 2006/07: None Required			
Local Government Impact: See Local Government Impact section			

Summary of Legislation

As introduced, the bill modifies the Public Employees' Retirement Association (PERA). Among other things, the bill:

- establishes a new defined benefit plan for PERA members hired on or after January 1, 2007, with separate contribution rates and retirement benefits;
- includes additional pretax contributions in the definition of "salary" for purposes of determining contributions beginning January 1, 2009; and
- accelerates Amortization Equalization Disbursements (AED) payments.

Background. PERA consists of four divisions - state, school, local government, and judicial - each of which includes a separate trust fund, amortization period, and membership. The current contribution rates for each division are shown in Table 1.

Table 1. PERA Contribution Rates for FY 2006-07		
Division	Employer Rate	Employee Rate
State	State Troopers 12.85%	10.00%
	All Others 10.15%	8.00%
School	10.15%	8.00%
Local Government	10.00%	8.00%
Judicial *	13.66%	8.00%

* The Judicial division includes judges only, not other court staff.

Retirement benefits are calculated based on an employee's age, years of service, and highest average salary (HAS). If a person meets the eligibility requirements (for most employees, age plus years of service equals 80), the retirement benefit is equal to 2.5 percent of HAS for each year of service, up to 100 percent. Within the state division, HAS is based on 3 years' of salary, but salary increases used in calculating an employee's HAS are limited to 15 percent per year for service credit earned during the last 3 years of membership. Retirement benefits for current retirees and persons hired before July 1, 2005, automatically increase each year by 3.5 percent per year, while benefits for members hired on or after July 1, 2005, are increased by the lesser of 3% per year or the rate of inflation.

Overall Program Changes. The bill divides PERA members into 2 groups of benefit recipients. Members hired before January 1, 2007, are called Pioneer members; those hired on or after January 1, 2007, are called Centennial members. A new reserve is established within each division for Centennial members, and the bill specifies the amounts that must be allocated to each reserve.

The bill increases AED payments to PERA beginning in 2008, as shown in Table 2.

Table 2. Estimated State AED Payments Under SB 06-174		
Year	Current	Proposed
2006	0.50	0.50
2007	1.00	1.00
2008	1.40	1.50
2009	1.80	2.00
2010	2.20	2.50
2011	2.60	3.00
2012	3.00	3.50

For members that retire on or after January 1, 2009, the bill limits annual salary increases used in the HAS calculation to 15% per year. It also reduces the maximum amortization period for considering PERA trust funds actuarially sound from 40 to 30 years. The PERA board of trustees is responsible for setting the cost to buy forfeited service credit at a level sufficient to pay the

actuarial liability associated with the purchase, as they currently do by policy. Starting January 1, 2007, all contributions made on behalf of members participating in the state's defined contribution plan must be delivered to PERA before being delivered to the state defined contribution plan.

Changes Affecting PERA Members. The bill modifies the benefits, contributions, and calculations for *all* PERA members as follows:

- limits annual salary increases used to calculate HAS for members who retire on or after January 1, 2009;
- expands the types of voluntary pretax contributions included in the definition of salary beginning January 1, 2009;
- sets the conditions for purchasing service credit based on those in effect at the time the member commences membership in PERA;
- reduces the monthly health care subsidy from \$230 to \$115 for all members who join PERA after January 1, 2007, and for other members who are not yet 45 years old by January 1, 2007; and
- reduces the portion transferred to PERA's Health Care Trust Fund from the amount paid by a member to purchase service credit.

For PERA members hired on or after January 1, 2007, the bill establishes retirement benefits based on the following:

- highest average salary (HAS) calculated over a 5-year period;
- 2.1% of a member's HAS multiplied by the member's years of service; and
- employee contribution rates that are 1 percent lower than current rates.

The bill establishes an "annual increase" reserve consisting of 0.5% of salaries to pay for annual cost-of-living adjustments to retirement benefits for members hired on or after January 1, 2007. Annual increases in benefits for these members would only be provided if the amount in the reserve is sufficient to fund the net present value of the actuarial liability associated with the increase. Just as with some current members, annual increases in retirement benefits would be capped at 3% per year or inflation, whichever is lesser. In no case, however, can an annual increase exhaust 10 percent or more of the market value of the reserve.

PERA must conduct an annual actuarial valuation of the program for new employees, beginning with an initial valuation to be conducted by January 1, 2007. In any year in which the valuation indicates a funded ratio of less than 90%, the bill requires that both employee and employer contributions be increased by 0.5% up to a maximum total increase of 3.0%. If the contribution rate increases reach the 3.0% cap and the valuation still indicates a funded ratio under 90%, the bill directs the PERA board of trustees to submit recommendations to the General Assembly to reduce benefits for members who are not eligible to retire. The bill specifies that benefits accrued prior to the reduction would not be affected. If the valuation indicates a funded ratio over 110%, the bill requires that contribution rates decrease by 0.5%.

State Revenues

By including additional pre-tax deductions in the definition of salary for PERA, the bill will increase the amount withheld from wages and contributed to PERA for some PERA-covered employees. This will also reduce taxable income, although the actual impact on state income tax collections has not been estimated.

State Expenditures

Overall, the bill is expected to increase state expenditures by \$1.2 million in FY 2007-08 and \$9.1 million in FY 2008-09. These costs are attributable to the increase in AED payments and the inclusion of certain voluntary pretax contributions in the definition of salary for PERA purposes.

Amortization Equalization Disbursements. The bill increases the statutorily-required AED payments, as shown in Table 2 below. Table 2 also shows the estimated cost of the increase to the state division.

Table 2. Estimated State AED Payments Under SB 06-174					
Year	Current	Proposed	Estimated Cost	Fiscal Year (FY)	FY Cost
2006	0.50	0.50	\$0	FY 2005-06	\$0
2007	1.00	1.00	\$0	FY 2006-07	\$0
2008	1.40	1.50	\$2,340,727	FY 2007-08	\$1,170,364
2009	1.80	2.00	\$4,892,120	FY 2008-09	\$3,616,424
2010	2.20	2.50	\$7,668,398	FY 2009-10	\$6,280,259
2011	2.60	3.00	\$10,684,635	FY 2010-11	\$9,176,517
2012	3.00	3.50	\$13,956,804	FY 2011-12	\$12,320,720

Including Pretax Contributions in Salary. The bill expands the types of voluntary pretax contributions included in the definition of salary, for purposes of both PERA and the state defined contribution plan beginning January 1, 2009. Under the bill, the salary used to calculate contributions would include amounts that members deduct from before-tax wages for flexible spending health plans and transportation plans. This will increase state contributions to PERA by an estimated \$5.4 million in FY 2008-09.

Public Employees' Retirement Association

The bill divides PERA members into 2 groups of benefit recipients, and makes several other changes. PERA members hired on or after January 1, 2007, would contribute less to PERA, but would also receive less in retirement benefits. The bill increases the AED payments to PERA beginning in 2008, increasing revenue to PERA. It also reduces the maximum amortization period

for considering PERA trust funds actuarially sound from 40 to 30 years. For employees hired on or after January 1, 2007, the bill allows for adjustments in both employer and employee contribution rates to ensure the trust fund has a funded ratio of at least 90 percent.

For members that retire on or after January 1, 2009, the bill extends the existing 15 percent limit on annual increases in salary used in the HAS calculation to include one year prior to the years included in the calculation. This provision will reduce future PERA obligations. In addition, the bill reduces the monthly health care subsidy from \$230 to \$115 for all members who join PERA after January 1, 2007, and for other members who are not yet 45 years old by January 1, 2007.

Local Government Impact

Local governments that participate in PERA, including most school districts, would experience impacts similar to those described above for the state.

State Appropriations

No new state appropriations are required for FY 2006-07.

Departments Contacted

PERA Personnel and Administration