

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

Drafting Number: LLS 06-0506
Prime Sponsor(s): Sen. Owen

Date: April 24, 2006
Bill Status: Senate SVMA
Fiscal Analyst: Chris Ward (303-866-5834)

TITLE: CONCERNING RETIREMENT BENEFIT PLANS FOR PUBLIC EMPLOYEES.

Fiscal Impact Summary	FY 2006/07	FY 2007/08	FY 2008/09
State Revenues			
State Expenditures			
Total	\$1,946,694	\$11,027,320	\$24,791,623
FTE Position Change	0.1 FTE	0.1 FTE	0.1 FTE
Effective Date: Upon signature of the Governor, except sections 5, 8, 15, and 18 - 21, which take effect January 1, 2007			
Appropriation Summary for FY 2006/07: See State Appropriations section			
Local Government Impact: See Local Government Impact section			

Summary of Legislation

As introduced, the bill modifies the Public Employees' Retirement Association (PERA), as well as the state-run defined contribution plan. 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, 2007;
- increases the retirement age for members who were hired before January 1, 2007, and who are less than 40 years of age when the act takes effect;
- allocates 1% of salary for state employees to PERA as a supplemental employer contribution for FY 2007-08 through FY 2009-10, to come from salary increases;
- restructures the PERA board of directors;
- allows any person working for a PERA eligible employer to choose between joining PERA's defined benefit plan, PERA's defined contribution plan, or the state's defined contribution plan instead of PERA; 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% of HAS for each year of service, up to 100%. 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% 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% 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 — those hired before January 1, 2007, and those hired on or after January 1, 2007. Beginning June 13, 2006, the bill reduces the maximum amortization period from 40 to 30 years for considering PERA's trust funds actuarially sound. In years in which this threshold is not met, the General Assembly is authorized to modify member and employer contribution levels as well as retirement benefits for PERA members who are not yet retired.

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

Effective January 1, 2007, the bill replaces the current 16-member PERA board of trustees with a new 11-member board. The new board would consist of the State Auditor; the State Treasurer; four PERA members (one from each division); one PERA retiree elected by PERA retirees; and four non-member trustees appointed by the Governor. If PERA is deemed to be actuarially unsound for 3 consecutive years, the existing board would be terminated and a new board would be elected and appointed, as applicable. The bill codifies PERA's policy that the cost to purchase service credit equal the actuarial cost of providing the future benefit resulting from the purchase and that the actuarial cost shall be determined by the member's age at the time of purchase and the division of PERA membership.

The bill requires the Legislative Council Staff, upon request of the Senate President and the Speaker of the House of Representatives, to contract for an actuarial analysis of PERA to determine whether increasing members' and retirees' benefits would cause PERA to become actuarially unsound. The bill specifies that the Attorney General shall not delegate his or her responsibilities as legal advisor to the board to any legal advisor or attorney hired by PERA. PERA's attorneys may still advise PERA staff, but not the board.

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

- requires that 1% of each member's salary for state employees be deducted from any salary increase and transferred to PERA as a supplemental contribution for FY 2007-08 through FY 2009-10;
- 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, 2007;
- increases the retirement age for members who were hired before January 1, 2007, and who are less than 40 years of age when the act takes effect; and
- allows any PERA employee to join the state's defined contribution plan instead of PERA.

Members who initially join PERA's defined contribution plan and then elect to join PERA's defined benefit plan instead would have the option to receive service credit for the total number of years and months that the member was in the defined contribution plan or to purchase service credit for the number of years and months that can be purchased with the value of the members defined contribution account.

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 for service retirement with a single life benefit payable for the life of the retiree;

- contribution rates of 7% for both employers and employees for **all** PERA members, regardless of division membership;
- for members with less than 35 years of service credit, eligibility for full retirement benefits when the member's age and total years of service reach 85, so long as the member is at least 60 years old;
- a lower level of retirement benefits for members that are not eligible for full retirement benefits;
- annual cost of living increases in retirement benefits that are only available when PERA is actuarially overfunded and 2/3 of the board approves the increase.

If the funded ratio of benefits for members hired on or after January 1, 2007, falls below 90%, and the General Assembly increases the employer contribution rate, the employee contribution rate must be increased by twice the increase for employers.

State Revenues

By reducing employee contributions to PERA for new hires, the bill will increase the amount withheld from taxable wages and also reduce taxable income. The actual impact on state and federal income tax collections has not been estimated.

State Expenditures

Overall, the bill is expected to increase state expenditures by \$1.9 million in FY 2006-07 and \$11.0 million in FY 2007-08. These costs are attributable to the creation of separate tiers for employees with reduced employer contribution rates, the increase in AED payments, the inclusion of certain voluntary pretax contributions in the definition of salary for PERA purposes, and the requirement that the Attorney General act as legal counsel for the board. The bill also allows the General Assembly to adjust contribution rates and retirement benefits if PERA's amortization period exceeds 30 years for purposes of determining actuarial soundness. Finally, the bill requires the Research Director of the Legislative Council, if requested by legislative leadership, to contract for an actuarial assessment of PERA related to a proposed increase in benefits, but it is assumed that the cost of this study would be paid by PERA.

Reduced Employer Contribution Rates for New Hires. The bill reduces the employer contribute rate to 7% of salary for all employees hired on or after January 1, 2007, which reduces state expenditures by the amounts shown in Table 3 for both the state and judicial divisions.

Table 3. Reduced State PERA Contributions for New Hires	
FY 2006-07	-\$7,313,890
FY 2007-08	-\$16,761,847
FY 2008-09	-\$21,096,367

Amortization Equalization Disbursements. The bill increases the statutorily-required AED payments, which will increase costs to the state division by the amounts shown in Table 4.

FY 2005-06	\$0
FY 2006-07	\$0
FY 2007-08	\$1,170,364
FY 2008-09	\$3,616,424
FY 2009-10	\$6,280,259
FY 2010-11	\$9,176,517
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. 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.

Attorney General as PERA Legal Counsel. The bill specifies that the Attorney General shall not delegate his or her responsibilities as legal advisor to the board to any legal advisor or attorney hired by PERA. This requirement will increase the workload of the Department of Law beginning in FY 2006-07 by an estimated 250 hours per year, or 0.1 FTE, at a cost \$16,113.

Public Employees' Retirement Association

The bill divides PERA members into 2 groups of benefit recipients and makes several other changes. The following provisions should either increase revenue or reduce obligations for PERA:

- one percent of salary increases would be credited to PERA as a supplemental employee contribution in FY 2007-08, FY 2008-09, and FY 2009-10;
- AED payments are increased beginning in 2008;
- the General Assembly may adjust contribution rates and future retirement benefits in certain circumstances;
- the retirement age is increased for new hires and other members under age 40;
- cost of living increases in retirement benefits are subject to certain conditions; and
- benefits for employees not eligible for full retirement benefits are further reduced and may affect retirement date decisions for affected employees.

The bill also expands eligibility for PERA's defined contribution plan, as an alternative to the defined benefit plan, to include all PERA employees instead of just new hires. To the extent that state employees exercise this option, the bill will reduce the funded ratio for all PERA defined benefit trust funds and make it less likely that the funds will meet the maximum amortization periods required in the bill.

Local Government Impact

Local governments that participate in PERA, including most school districts, would experience impacts similar to those described above for the state. However, the allocation of one percent of salary to PERA from salary increases for FY 2007-08 through FY 2009-10 would not apply to local governments.

State Appropriations

This fiscal note implies that the Department of Law will require spending authority for \$16,113 transferred from PERA for legal services, as well as 0.1 FTE. In addition, several appropriations adjustments will be required for FY 2006-07. These amounts will be provided in a revised fiscal note.

Departments Contacted

Law	Legislative Council Staff
PERA	Personnel and Administration
Revenue	

Omissions and Technical or Mechanical Defects

The compensation for PERA trustees is left blank on Page 11, lines 18 and 21.