COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

**FISCAL NOTE**

L.R. No.: 1807-01
Bill No.: SB 475
Subject: Retirement - State; Retirement Systems and Benefits - General; Retirement - Local Government; Retirement Schools; Liability; Boards, Commissions, Committees, Councils; Kansas City; Saint Louis
Type: Original
Date: April 8, 2013

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Bill Summary: This proposal mandates that certain retirement plans shall be one hundred percent funded in five years.

**FISCAL SUMMARY**

| ESTIMATED NET EFFECT ON GENERAL REVENUE FUND | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2014 | FY 2015 | FY 2016 |
| General Revenue | $0 | ($433,594,230) | ($448,421,139) |
| **Total Estimated Net Effect on General Revenue Fund** | **$0** | **($433,594,230)** | **($448,421,139)** |

| ESTIMATED NET EFFECT ON OTHER STATE FUNDS | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2014 | FY 2015 | FY 2016 |
| Road Fund | ($220,012,605) | ($220,012,605) | ($220,012,605) |
| Other | $0 | ($130,078,269) | ($134,526,342) |
| **Total Estimated Net Effect on Other State Funds** | **($220,012,605)** | **($350,090,874)** | **($354,538,947)** |

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 14 pages.

| ESTIMATED NET EFFECT ON FEDERAL FUNDS | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2014 | FY 2015 | FY 2016 |
| Federal Funds | $0 | ($158,984,551) | ($164,421,084) |
| | | | |
| **Total Estimated Net Effect on All Federal Funds** | **$0** | **($158,984,551)** | **($164,421,084)** |

| ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE) | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2014 | FY 2015 | FY 2016 |
| | | | |
| | | | |
| **Total Estimated Net Effect on FTE** | **0** | **0** | **0** |

☒ Estimated Total Net Effect on All funds expected to exceed $100,000 savings or (cost).

☒ Estimated Net Effect on General Revenue Fund expected to exceed $100,000 (cost).

| ESTIMATED NET EFFECT ON LOCAL FUNDS | | | |
|---|---|---|---|
| FUND AFFECTED | FY 2014 | FY 2015 | FY 2016 |
| **Local Government** | **(Greater than $1,938,621,741)** | **(Greater than $1,811,074,501)** | **(Greater than $1,814,980,072)** |

## FISCAL ANALYSIS

ASSUMPTION

Officials from the **Police Retirement System of St. Louis** assume this proposal would require the funding of all accrued liabilities of the fifteen public pension systems noted in the language. The direct fiscal impact to the system would be to increase the sponsor's contribution by approximately $50 million each year for the next five years, which would not take into account the required increases for the Fireman's Retirement System of St. Louis. The passage of this proposal would consume more than one-quarter of all revenues for the City of St. Louis on pension costs.

Officials from **MoDOT and Patrol Employees Retirement System (MPERS)** provided a report from their actuary which contains the results of a supplemental actuarial valuation of the proposal. The major provisions affecting MPERS that were considered, were:

- Shortening the amortization period to ensure that the funded status reached 100% by June 30, 2018;
- Freezing benefit accruals during any plan year where the funded status was below 80% at the beginning of the plan year.

The valuation was based upon data furnished by MPERS for the June 30, 2012 valuation. Actuarial methods and assumptions, except where otherwise noted, were the same as those used in the last regular annual actuarial valuation as of June 30, 2012. In particular:

- The assumed rate of interest was 8.25%.
- The valuation method was the entry-age actuarial cost method.
- The amortization period was 12 years for unfunded retiree liabilities and 27 years for unfunded active liability prior to the proposed change.
- Amortizations were calculated assuming payroll would increase 1.5% for each of the first two years and 3.75% per year, thereafter.
- Price inflation is assumed to be 3.25% per year.

ASSUMPTION (continued)

A brief summary of the data used in this valuation is presented below.

| Active and Retiree | | | | |
|---|---|---|---|---|
| Employee Group | Number | Covered Payroll/Annual Benefits | Average Age (Years) | Average Service (Years) |
| MoDot | 5,115 | $213,982,134 | 45.2 | 14.3 |
| Civilian Patrol | 1,128 | 42,605,045 | 44.7 | 12.3 |
| Uniformed Patrol | 1,215 | 72,705,989 | 39.6 | 14.4 |
| Total: | 7,458 | $329,293,168 | 44.2 | 14.0 |
| Retirees and Beneficiaries | 8,055 | $201,906,768 | 70.1 | N/A |

This proposed legislation is silent on a number of issues that could affect the valuation. After discussion with MPERS staff, our actuary, Gabriel Roeder Smith & Company (GRS) made assumptions about those issues in order to evaluate the financial impact. Should the actual implementation of this legislation differ from those assumptions (if passed), then the actual financial impact may be different than shown herein. Those issues include:

The effective date of the legislation

- GRS valued the proposed changes as if they became effective on July 1, 2012. Given the lag between the valuation date and the contribution effective date, this allows for a 5-year amortization (financing period) of the unfunded actuarial accrued liabilities as of June 30, 2012.
- The June 30, 2012 valuation determines the employer contribution rates for fiscal year 2014. These rates have already been adopted by the Board. GRS assumed that the fiscal year 2014 employer contributions would be changed if this legislation passes. If this is not the case, a shorter amortization and higher contribution rates would be needed.

Method of financing

- MPERS' statute requires level percent of payroll financing, but is silent on the actual amortization period to be used in each valuation. GRS therefore believes this would be set by Board policy.

ASSUMPTION (continued)

- GRS assumed that the amortization period would start at 5 years (in the 2012 valuation) and reduce 1 year in each future year (i.e., 5, 4, 3, 2, 1).
- A different set of amortization periods in future valuations could be used and still satisfy the proposed legislation's requirement. For example, the amortization periods used in each valuation, beginning with the 2012 valuation could be 2, 3, 2, 4, 1 or 30, 30, 30, 30, 1 or any other combination of periods that ends with a 1-year amortization in the June 30, 2017 valuation. If the Board adopts any set of amortization periods other than what was assumed (5, 4, 3, 2, 1), then the financial effects will be different than shown herein.

Benefit freeze

- Section 5 states: "When a statutory retirement plan funded ratio falls below eighty percent, benefit accruals under the plan shall cease as of the valuation date for the plan year." GRS assumed that a statutory plan that starts under the 80% funding level would have benefit accruals frozen immediately. For purposes of this valuation, GRS assumed the first plan year of the freeze would be FY2013 for MPERS.
- Based on a simplified projection, GRS determined that the benefit accruals will be frozen for 3 years (FY2013, FY2014, and FY2015), using a 5 year closed amortization period. If a different pattern of amortization periods is selected by the Board, the number of years the benefit freeze is expected to be in effect could be different.
- GRS assumed that the benefit freeze ends the year following attainment of an 80% funded ratio. However, this is not actually specified in the legislation.
- The manner in which the benefit freeze is actually administered can affect the reduction in liabilities as a result of the freeze. GRS valued the freeze by freezing FAP and service for the 3-year period following the valuation date.

ASSUMPTIONS (continued)

Employer Contributions and Valuation Results*
After Proposed Legislation
Expressed as %'s of Active Member Pays

| Contribution for | Non-Uniformed Civilian Patrol | Non-Uniformed MoDOT | Non-Uniformed Total | Uniformed Patrol | Total |
|---|---|---|---|---|---|
| Normal Cost | 9.46% | 9.46% | 9.46% | 15.27% | 10.75% |
| Expenses and Disability Premium | 1.43% | 1.43% | 1.43% | 1.43% | 1.43% |
| UAAL % | 107.09% | 107.09% | 107.09% | 108.06% | 107.31% |
| Total Employer Rate | 117.98% | 117.98% | 117.98% | 124.76% | 119.49% |
| UAAL $ | n/a | n/a | $1,261,911,475 | $375,830,991 | $1,637,742,466 |
| Funded Status | | | | | 48.3% |
| Projected Employer Dollar Contributions FY 14 | $54,106,025 | $252,456,122 | $306,562,147 | $97,638,649 | $404,200,796 |

* Computed as a level percent of payroll for 5 years. Contributions will then reduce to the normal cost (plus amortization of future gains and losses).

Actuarial Statement

Employer Contributions and Valuation Results
Before Proposed Legislation
Expressed as %'s of Active Member Pays

| Contribution for | Non-Uniformed Civilian Patrol | Non-Uniformed MoDOT | Non-Uniformed Total | Uniformed Patrol | Total |
|---|---|---|---|---|---|
| Normal Cost | 11.07% | 11.07% | 11.07% | 17.34% | 12.47% |
| Expenses and Disability Premium | 1.43% | 1.43% | 1.43% | 1.43% | 1.43% |
| UAAL % | 41.75% | 41.75% | 41.75% | 36.46% | 40.54% |
| Total Employer Rate | 54.25% | 54.25% | 54.25% | 55.23% | 54.44% |
| UAAL $ | n/a | n/a | $1,362,414,960 | $412,830,098 | $1,775,245,058 |
| Funded Status | | | | | 46.3% |
| Projected Employer Dollar Contributions FY 14 | $24,879,233 | $116,085,308 | $140,964,541 | $43,223,650 | $184,188,191 |

ASSUMPTIONS (continued)

Based on the tables above, **Oversight** assumes the following to be the changes in employer contributions annually for five years. Oversight also assumes this will change the Unfunded Accrued Actuarial Liabilities (UAAL) annually.

Civilian Patrol: 29,226,792
MoDot: 136,370,814
Uniformed Patrol: 54,414,999
Total: $220,012,605

Overall UAAL change: $137,502,592 (2014)

In addition, MPERS states that the administration of these provisions will require programming of their pension administration system, which could incur a substantial cost.

Officials from the **Missouri State Employees' Retirement System (MOSERS)** assume that the proposal would require the Missouri State Employees' Plan and the Judicial Plan to achieve and maintain a funded ratio of assets, as defined in Section 105.660 RSMo, equaling 100% by the first plan year ending January 1, 2018.

MSEP Projected DB Employer Contributions

| Fiscal Year | Val Payroll Projected | Before Proposed Changes | | Estimated Impact of Proposed Changes | | After Proposed Change | |
|---|---|---|---|---|---|---|---|
| | | Rate | Dollars | Total Rate | Total Dollars | Rate | Dollars |
| 2012 | $1,864,069,493 | | | | | | |
| 2013 | 1,919,991,578 | | | | | | |
| 2014 | 1,977,591,325 | 16.98% | $ 335,795,007 | 0.00% | $ - | 16.98% | $ 335,795,007 |
| 2015 | 2,036,919,065 | 16.40% | 334,054,727 | 32.08% | 653,443,636 | 48.48% | 987,498,363 |
| 2016 | 2,098,026,637 | 15.89% | 333,376,433 | 32.21% | 675,774,379 | 48.10% | 1,009,150,812 |
| 2017 | 2,160,967,436 | 15.40% | 332,788,985 | 32.35% | 699,072,966 | 47.75% | 1,031,861,951 |
| 2018 | 2,225,796,459 | 14.94% | 332,533,991 | 32.48% | 722,938,690 | 47.42% | 1,055,472,681 |
| 2019 | 2,292,570,353 | 14.51% | 332,651,958 | (8.90)% | (204,038,761) | 5.61% | 128,613,197 |
| 2020 | 2,361,347,464 | 14.11% | 333,186,127 | (8.75)% | (206,617,903) | 5.36% | 126,568,224 |
| 2021 | 2,432,187,888 | 13.72% | 333,696,178 | (8.61)% | (209,411,377) | 5.11% | 124,284,801 |
| 2022 | 2,505,153,525 | 13.35% | 334,437,996 | (8.48)% | (212,437,019) | 4.87% | 122,000,977 |
| 2023 | 2,580,308,131 | 13.00% | 335,440,057 | (8.35)% | (215,455,729) | 4.65% | 119,984,328 |

ASSUMPTIONS (continued)

Below are the estimated changes in employer contributions, based on the actuarial report from Gabriel Roeder Smith & Company (GRS).

Missouri State Employees' Plan:

The shortening of the amortization period results in an increase in the projected employer contribution rate of 32.08% in 2015 and 32.21% in 2016.

Judicial Plan:

| | | Judicial Plan Projected DB Employer Contributions | | | | | |
|---|---|---|---|---|---|---|---|
| | | Before Proposed Changes | | Estimated Impact of Proposed Changes | | After Proposed Change | |
| Fiscal Year | Val Payroll Projected | Rate | Dollars | Total Rate | Total Dollars | Rate | Dollars |
| 2012 | $45,835,501 | | | | | | |
| 2013 | 47,210,566 | | | | | | |
| 2014 | 48,626,883 | 59.69% | $ 29,025,386 | 0.00% | $ 0 | 59.69% | $ 29,025,386 |
| 2015 | 50,085,690 | 58.47% | 29,285,103 | 138.19% | 69,213,414 | 196.66% | 98,498,517 |
| 2016 | 51,588,260 | 57.19% | 29,503,326 | 138.78% | 71,594,187 | 195.97% | 101,097,513 |
| 2017 | 53,135,908 | 55.92% | 29,713,600 | 139.36% | 74,050,201 | 195.28% | 103,763,801 |
| 2018 | 54,729,985 | 54.66% | 29,915,410 | 139.87% | 76,550,830 | 194.53% | 106,466,240 |
| 2019 | 56,371,885 | 53.55% | 30,187,144 | (38.35)% | (21,618,618) | 15.20% | 8,568,526 |
| 2020 | 58,063,041 | 52.50% | 30,483,097 | (37.67)% | (21,872,348) | 14.83% | 8,610,749 |
| 2021 | 59,804,933 | 51.55% | 30,829,443 | (37.09)% | (22,181,650) | 14.46% | 8,647,793 |
| 2022 | 61,599,081 | 50.59% | 31,162,975 | (36.52)% | (22,495,984) | 14.07% | 8,666,991 |
| 2023 | 63,447,053 | 49.68% | 31,520,496 | (35.95)% | (22,809,216) | 13.73% | 8,711,280 |

The shortening of the amortization period results in an increase in the projected employer contribution rate of 138.19% in 2015 and 138.78% in 2016.

**Oversight** assumes the costs estimated by MOSERS would be distributed across state funds in the following percentages; general revenue 60%, other state funds 18% and federal funds 22%.

Officials from the **Joint Committee on Public Retirement** state that their review of the proposal indicates that such legislation may constitute a "substantial proposal change" in future plan benefits as defined in Section 105.660(10), RSMo. It is impossible to accurately determine the fiscal impact of this proposed legislation without an actuarial cost statement prepared.

ASSUMPTIONS (continued)

Officials from the **Sheriffs' Retirement System** assume this proposal would require an additional contribution of $350,000 each year through January 1, 2018 for the system to be 100% funded.

Officials from the **Public School Retirement System of the City of St. Louis** believes this proposal constitutes a substantial proposed change in future benefits. Due to lack of a cost statement, the additional costs of the proposed legislation are currently unknown.

Officials from the **County Employees Retirement Fund (CERF)** assume the proposal will result in a cost to their foundation. The 2014 amount of $101,112,000 will allow the fund to reach a funded ration of 100% as of January 1, 2018. The calculation of the 2014 amount is based on the actuarial assumptions used in the most recent actuarial report, which is as of July 1, 2012.

In addition, CERF states that part of their revenue supports a matching contribution to the CERF defined contribution plan. CERF revenues are predictable. Therefore, the actuary is able to design a pension benefit formula that can be supported by the expected revenues. CERF determines its revenue first and then determines the benefits. Other plans first determine their benefits, and then they depend on the taxpayers for the revenue.

Officials from the **Missouri Local Government Employees Retirement System** assume that in order to comply with the proposal they would be required to adjust all employer contributions to assure 100% by June 30, 2018. Current amortization periods range from 15 to 30 years per section 70.730, RSMo. Full funding by 2018 would require the following additional contributions: approximately $261 million in 2014, approximately $270 million in 2015 and approximately $280 million in 2016. In addition, the shorter amortization periods indicated in Section 105.686 RSMo introduces significant volatility in future employer contributions.

Officials from the **Kansas City Public School Retirement System (KCPSRS)** assume that in order to fulfill the requirements of the five year amortization period employer contributions would need to be increased through statute to achieve the levels noted above. The current statutory employer contribution rate is 7.5%.

ASSUMPTIONS (continued)

They did provide estimates of increased employer contributions and contribution rates needed to make the system 100% funded by 2018:

2013 - $57,773,433 Contribution rate - 36.75%
2014 - $59,159,741 Contribution rate - 37.09%
2015 - $64,724,501 Contribution rate - 39.78%
2016 - $75,630,072 Contribution rate - 45.43%
2017 - $82,636,374 Contribution rate - 48.44%

**Oversight** assumes, for fiscal note purposes, that the necessary statutory changes will be enacted if this proposal becomes law.

Officials from the **Public School and Education Employees Retirement System** state that the result of this proposal is a significant increase in annual cost over the next five years, followed by an annual savings for the next 25 years. An increase in contributions of approximately $1.467 billion in FY 2014, $1.426 billion in FY 2015, and $1.409 billion in FY 2016 is expected.

**Oversight** has received a response from nine of the fifteen retirement systems listed in the proposal.

**Oversight** will assume an unknown cost to the Kansas City Police Retirement System (3) & (4), the Prosecuting Attorneys and Circuit Attorneys Retirement System (9), as well as the Firemen's Retirement System of St. Louis (13).

| FISCAL IMPACT - State Government | FY 2014 (10 Mo.) | FY 2015 | FY 2016 |
|---|---|---|---|
| **GENERAL REVENUE FUND** | | | |
| Costs - MOSERS Increased employer contributions for Missouri State Employee Plan | $0 | ($392,066,182) | ($405,464,627) |
| Costs - MOSERS Increased employer contributions for Judicial Plan | $0 | ($41,528,048) | ($42,956,512) |
| **ESTIMATED NET EFFECT ON GENERAL REVENUE FUND** | **$0** | **($433,594,230)** | **($448,421,139)** |

| FISCAL IMPACT - State Government (continued) | FY 2014 (10 Mo.) | FY 2015 | FY 2016 |
|---|---|---|---|
| **ROAD FUND** | | | |
| Costs - MPERS | | | |
| Increased employer contributions | ($220,012,605) | ($220,012,605) | ($220,012,605) |
| **ESTIMATED NET EFFECT ON ROAD FUND** | **($220,012,605)** | **($220,012,605)** | **($220,012,605)** |
| **FEDERAL FUNDS** | | | |
| Costs - MOSERS | | | |
| Increased employer contributions for Missouri State Employee Plan | $0 | ($143,757,600) | ($148,670,363) |
| Costs - MOSERS | | | |
| Increased employer contributions for Judicial Plan | $0 | ($15,226,951) | ($15,750,721) |
| **ESTIMATED NET EFFECT ON FEDERAL FUNDS** | **$0** | **($158,984,551)** | **($164,421,084)** |
| **OTHER STATE FUNDS** | | | |
| Costs - MOSERS | | | |
| Increased employer contributions for Missouri State Employee Plan | $0 | ($117,619,854) | ($121,639,388) |
| Costs - MOSERS | | | |
| Increased employer contributions for Judicial Plan | $0 | ($12,458,415) | ($12,886,954) |
| **ESTIMATED NET EFFECT ON OTHER STATE FUNDS** | **$0** | **($130,078,269)** | **($134,526,342)** |

| FISCAL IMPACT - Local Government | FY 2014 (10 Mo.) | FY 2015 | FY 2016 |
|---|---|---|---|
| **POLITICAL SUBDIVISIONS** | | | |
| Costs - St. Louis - STLPD Retirement System (14) & Fireman's (13) Increased employer contributions | (Greater than $50,000,000) | (Greater than $50,000,000) | (Greater than $50,000,000) |
| Costs - Counties - Sheriffs' Retirement System Increased employer contributions | ($350,000) | ($350,000) | ($350,000) |
| Costs - Counties - CERF Increased employer contributions | ($101,112,000) | $0 | $0 |
| Costs - Municipalities - LAGERS Increased employer contributions | ($261,000,000) | ($270,000,000) | ($280,000,000) |
| Costs - Kansas City - KCPSRS Increased employer contributions | ($59,159,741) | ($64,724,501) | ($75,630,072) |
| Costs - School Districts - PSRS Increased employer contributions | ($1,467,000,000) | ($1,426,000,000) | ($1,409,000,000) |
| Costs - St. Louis School District - Increased employer contributions (15) | (Unknown) | (Unknown) | (Unknown) |
| Costs - Kansas City - Police Retirement System (3) & (4) - increased employer contributions | (Unknown) | (Unknown) | (Unknown) |
| Costs - Counties - Prosecuting Attorneys and Circuit Attorney retirement system (9) - increased employer contributions | (Unknown) | (Unknown) | (Unknown) |
| **ESTIMATED NET EFFECT ON POLITICAL SUBDIVISIONS** | **(Greater than $1,938,621,741)** | **(Greater than $1,811,074,501)** | **(Greater than $1,814,980,072)** |

LO:LR:OD

FISCAL IMPACT - Small Business

No direct fiscal impact to small businesses would be expected as a result of this proposal.

FISCAL DESCRIPTION

This proposal provides that certain retirement plans shall be one hundred percent funded in five years. If the specified plans do not maintain a hundred percent funded ratio then the plans cannot adjust or increase benefits. The proposal also states that when a plan falls below eighty percent then benefit accruals shall cease.

When the annual plan investment rate of return falls below zero percent then neither the plan, governing body, nor plan employees shall be held civilly liable for the loss of funds or failure to maintain the one hundred percent funded ratio.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Joint Committee on Public Retirement
County Employees Retirement Fund
Missouri State Employees Retirement System
Missouri Local Government Employees Retirement System
MoDOT and Patrol Employees Retirement System
St. Louis Police Retirement System
Public School Retirement System of St. Louis
Kansas City Public School Retirement System
Public School and Education Employees Retirement System

Ross Strope
Acting Director

LO:LR:OD

April 8, 2013

LO:LR:OD