

URS Fiscal Analysis of 2016 H.B. 86

This document has been prepared by the Utah Retirement Systems (URS) based on information and analysis received from its consulting actuary, Gabriel Roeder Smith & Company.

Summary of Fiscal Impact

If enacted, H.B. 86, Postretirement Employment Restrictions, has the following fiscal impact on URS:

Increase in unfunded actuarial accrued liability:	Increase in annual cost for all participating employers:		Increase in actuarially determined contribution rates:
\$223.4 million	Total: \$25.7 million		See Exhibit 3 for detailed information about the contribution rate increases, but some examples are: <ul style="list-style-type: none"> • Tier I Public Employees Noncontributory Retirement System, State and School Fund: 0.31% increase • Tier I Public Safety Noncontributory Funds: increases ranging from .55% to 1.23% • Tier I Firefighters' Retirement System: <ul style="list-style-type: none"> ○ Division A: 1.03% increase ○ Division B: 1.33% increase
	Amount of the annual cost increase financed by requiring employers to pay the full contribution rate (rather than just the amortization rate) on the salary of reemployed retirees: <div style="text-align: right;">\$9.142 million</div>	Amount of the annual cost increase financed by increases to the actuarially determined employer contribution rates: <div style="text-align: right;">\$16.558 million</div>	

If this legislation becomes enacted, there would be a \$25.7 million increase in the annual cost for the participating employers in URS. Also, the collective unfunded actuarial accrued liability of the participating employers will increase by \$223.4 million due to this legislation. Please refer to Exhibit 4 for the impact on the unfunded actuarial accrued liability and funded ratio for each fund.

The actuary also separately analyzed the financial effect of the provision that requires employers of working retirees to contribute the Board certified contribution rate, rather than the amortization rate that is currently contributed on the payroll of working retirees. The increased contributions on the payroll of the working retirees would finance a portion, but not all, of the fiscal impact of the benefit improvement. Specifically, the actuary determined that this modification would finance 35%, or \$9.1 million of the total \$25.7 million in increased annual cost. Exhibit 3 provides additional information by fund.

If enacted, this legislation would increase the actuarially determined contribution rate for the Noncontributory State and School fund, Fund 16, by 0.31%. The actuarially determined contribution rates for the Noncontributory Public Safety Funds would experience increases ranging from 0.55% to 1.23% of pay, and the contribution rates for the Division A and B Firefighter funds would increase by 1.03% and 1.33%, respectively. The contribution rates for both the Tier II Hybrid Plans would also increase, but they would continue to remain noncontributory. However, since the employer's cost is fixed at 10% of pay (12% of pay for public safety and fighters), the increased cost of the defined benefit plan would decrease the allocation to the members' defined contribution account. Please refer to the Exhibit 3 for detailed cost impact information and contribution rate impacts for each fund.

Proposed Legislative Provisions

This particular bill would exempt a retired member from the postretirement reemployment earnings limit if they become reemployed at a different agency after 60 days following their initial retirement date. Currently URS will suspend the retirement allowance for members who become reemployed between 60 days after but within one year of their initial date of retirement if the member's compensation during the calendar year exceeds the lesser of \$15,000 or 50% of their final average salary (FAS).

The proposed legislation would exempt a retiree from the earnings limit (\$15,000 or 50% of FAS) as long as: (1) the reemployment occurs at least 60 days from the retiree's initial retirement date, (2) the retiree is reemployed by a different agency, and (3) the retiree does not receive any employer paid retirement service credit or retirement related contributions from the participating employer. This legislation also requires employers to pay the full contribution rate on the salary of the eligible exempt retiree. These changes become effective immediately upon enactment.

Discussion and Actuarial Analysis

For more background information, general discussion, and analysis of postretirement reemployment restrictions and the fiscal impact of potential changes to the working after retirement provisions, please see the letter from Gabriel Roeder Smith & Company to URS Executive Director Daniel Andersen dated September 23, 2015, including the exhibits. This letter titled, "Actuarial Analysis: Potential Changes to Working After Retirement Provisions" was presented at the Legislature's Retirement Working Group meeting on September 24, 2015 and is available online at <http://le.utah.gov/interim/2015/pdf/00004225.pdf>. This Working Retiree Analysis reflects the actuary's 2015 study of historical experience as well as the most recent actuarial valuation of URS.

The provision changes modeled herein provide members significant opportunity to increase their personal financial resources late in their career by encouraging members to commence their retirement benefit and continue to participate in the workforce. As a result, we must anticipate the change in the retirement behavior and the age members commence their retirement allowance to identify the financial impact of the modifications to the working after retirement provisions.

To model the anticipated change in retirement behavior, we analyzed the historical working retiree behavior for members retiring four and half years prior to and four and half years after the enactment of SB 43, the working retiree reform legislation enacted during the 2010 legislation and became effective July 1, 2010. Based on this analysis, as well as our prior understanding of the overall change in retirement behavior as a result of performing an experience study in 2014, we have increased the

retirement rates below age 65 for public employees and below age 60 for public safety members and firefighters.

This legislation requires employers to pay the full contribution rate (rather than just the amortization rate) on the salary of the eligible exempt retirees, which would finance a portion, but not all, of the fiscal impact of the benefit improvement. There are a couple of characteristics to note about this financing mechanism. First, this financing arrangement places a larger portion of the financial cost on those employers who utilize working retirees in their workforce. In other words, rather than applying the cost increase proportionately to all employers as a percentage of payroll, this “user fee” requires those employers who utilize working retirees in their workforce to pay a slightly higher portion of the benefit enhancement. However, this surcharge does not cover all of the cost of the changes to the provisions. All employers would experience some increase in their contribution rates; even those employers that do not rehire retirees.

Another characteristic of this financing arrangement is the working retiree’s benefit is no longer fully funded at the time they commence their retirement benefit and the retirement system has increased reliance on those anticipated contributions as a working retiree to avoid an actuarial loss due to their retirement. As a result, it will become even more important for URS to have appropriate employer reporting processes in place for working retirees to ensure the employers are not under reporting their working retiree payroll in order for URS to collect the appropriate employer contributions on the payroll of their working retirees.

Also note that the actuarially determined contribution rates would continue to remain below the Board certified rates that are in effect for fiscal year 2017. In accordance with Utah Code Subsection 49-11-301(5), the Board has the option of maintaining the current certified contribution rates or increasing the certified contribution rates to reflect the increased cost due to this legislation. We suggest the Board discuss and consider increasing the contribution rates. The alternative is to maintain the current certified rates and extend the projected date the funds will attain a 100% funded status.

Data and Assumptions

This modeled analysis is based on the member and financial data that were used to prepare the January 1, 2015 actuarial valuation which was presented and adopted by the Board in August 2015.

To model the anticipated change in retirement behavior, we have assumed that the normal retirement rates for state and local government employees would increase by 4% (i.e. add 4%) at each age under age 65. On the other hand, where historical return to work behavior was found to be more prevalent for public educators, normal retirement rates for this employee group were increased by 6% at each age under age 65.

Similarly, the retirement rates for public safety members were increased by 6% at each age prior to age 60, whereas firefighters were only increased by 2% at each age prior to age 60.

Other Actuarial Comments

In our opinion, removing the earnings limit for retirees who seek reemployment between 60 and 365 days of their initial retirement date provides significant flexibility for members to commence their retirement benefit and shortly thereafter reenter the workforce. Due to Utah’s high urbanization rate, the requirement for retirees to seek reemployment at a different agency in order to continue receiving their retirement allowance, will be a relatively low hurdle for most employee groups. Since there are

numerous State agencies, often with several agencies operating within a single building or complex, retired State employees will have opportunity to find an employment position that satisfies this requirement. In application, retired city and county employees, including public safety officers and firefighters, will need to seek employment at a different municipality or county. The different agency provision could be slightly more problematic for school teachers since they will have to seek employment at a different school district. However, we also expect a majority of the retired school teachers can seek suitable employment that is within a 30 to 45 minute commute from their current residence.

Note, the different agency provision could be problematic for some employers because of the inability to utilize these retirees in the workforce to provide valuable services for certain essential tasks or projects. For instance, under these provisions, school districts would be unable to utilize recently retired teachers from their school districts as substitute teachers during the school year following the member's retirement.

Our calculations are based upon assumptions regarding future events, which may or may not materialize. Please bear in mind that actual results could deviate significantly from our projections, depending on actual plan experience. This information is intended to describe the financial and actuarial effect of the proposed plan changes on URS only. Changes in reemployment provisions could impact the cost of other benefit programs, such as post-retirement health benefits. Our analysis does not include this possible effect.

While the actuarially determined contribution rates would continue to remain below the Board certified rates that are in effect for fiscal year 2017, Utah Code Subsection 49-11-301(5) provides the Board the ability to maintain the current certified contribution rates or increase the certified contribution rates to reflect the increased cost of the benefit enhancement. We suggest the Board discuss and consider increasing the contribution rates. The alternative is to maintain the current certified rates and extend the projected date the funds will attain a 100% funded status.

It should be noted that we are neither for nor against the proposed changes. Return to work rules for retirees is a policy decision for the Legislature and employers. Our goal is to inform the stakeholders of the impact on URS of changes to these rules.

Administrative Cost Analysis

As with all bills that alter benefit design or make substantive benefit modifications, implementation of H.B. 86 will likely result in some administrative costs. However, such costs will be handled within existing budgets, will not result in direct, measurable costs for URS, and will not result in an increase to actuarially determined contribution rates in addition to those discussed above resulting from the benefit modifications.

Exhibit 3

Impact on Annual Cost and Contribution Rates if Employers Contribute the Full Board Certified Rate on the Payroll of Working Retirees (\$ in thousands)

Fund/Division (1)	Impact on Annual Cost			Impact on Actuarially Determined Rate		
	Total Cost Increase (2)	Cost Increase Financed by Contributions on Working Retiree Pay (3)	Cost Increase Financed by the Employer Certified Rates (4)	Total Increase in Actuarially Determined Rate (5)	Decrease Due to Increased Contributions on Working Retiree Pay (6)	Net Increase in Actuarially Determined Rate (7)
I. Public Employees Contributory						
A. Local Government	\$ 162	\$ 43	\$ 119	0.32%	-0.07%	0.25%
B. State and School	122	45	77	0.41%	-0.11%	0.30%
II. Public Employees Noncontributory						
A. Local Government	2,990	718	2,272	0.32%	-0.07%	0.25%
B. State and School	12,000	3,269	8,731	0.41%	-0.10%	0.31%
III. Public Safety Contributory						
A. State	3	1	2	2.10%	-0.34%	1.76%
B. Other Division A (2.5% COLA)	54	14	40	1.96%	-0.42%	1.54%
C. Other Division A (4% COLA)	7	2	5	2.30%	-0.58%	1.72%
D. Other Division B (2.5% COLA)	1	0	1	1.62%	-0.15%	1.47%
E. Other Division B (4% COLA)	4	2	2	1.97%	-0.83%	1.14%
IV. Public Safety Noncontributory						
A. State	2,152	1,276	876	1.98%	-0.99%	0.99%
B. Other Division A (2.5% COLA)	2,162	1,294	868	1.94%	-1.00%	0.94%
C. Other Division A (4% COLA)	730	421	309	2.22%	-1.13%	1.09%
D. Salt Lake City	619	372	247	2.20%	-1.15%	1.05%
E. Ogden	117	71	46	2.07%	-1.09%	0.98%
F. Provo	114	67	47	2.20%	-1.10%	1.10%
G. Logan	58	35	23	2.43%	-1.20%	1.23%
H. Bountiful	30	19	11	1.66%	-0.98%	0.68%
I. Other Division B (2.5% COLA)	902	714	188	1.67%	-1.12%	0.55%
J. Other Division B (4% COLA)	93	55	38	1.98%	-1.05%	0.93%
V. Firefighters						
A. Division A	371	85	286	1.30%	-0.27%	1.03%
B. Division B	1,429	266	1,163	1.61%	-0.28%	1.33%
VI. Judges	0	0	0	0.00%	0.00%	0.00%
V. Tier II - Hybrid Plans						
A. Public Employees	947	186	761	0.05%	-0.02%	0.03%
B. Public Safety and Firefighter	633	187	446	0.42%	-0.22%	0.20%
IV. Grand Total	\$ 25,700	\$ 9,142	\$ 16,558			

Exhibit 4

Impact on Unfunded Actuarial Accrued Liability and Funded Ratio by Fund Determined on an Actuarial Value of Asset Basis (\$ in thousands)

Fund/Division (1)	Unfunded Actuarial Accrued Liability			Funded Ratio		
	Current (2)	Proposed Legislation (3)	Increase (4)	Current (5)	Proposed Legislation (6)	Decrease (7)
I. Public Employees Contributory						
A. Local Government	\$ 48,655	\$ 50,194	\$ 1,539	89.8%	89.6%	-0.20%
B. State and School	48,064	49,301	1,237	94.1%	94.0%	-0.10%
II. Public Employees Noncontributory						
A. Local Government	572,485	602,788	30,303	87.0%	86.4%	-0.60%
B. State and School	2,750,262	2,870,450	120,187	85.5%	84.9%	-0.60%
III. Public Safety Contributory						
A. State	250	272	22	99.5%	99.4%	-0.10%
B. Other Division A (2.5% COLA)	2,949	3,388	439	97.7%	97.3%	-0.40%
C. Other Division A (4% COLA)	394	452	58	98.5%	98.2%	-0.30%
D. Other Division B (2.5% COLA)	63	70	8	99.8%	99.8%	0.00%
E. Other Division B (4% COLA)	282	318	36	96.6%	96.2%	-0.40%
IV. Public Safety Noncontributory						
A. State	213,206	231,517	18,311	81.0%	79.7%	-1.30%
B. Other Division A (2.5% COLA)	117,224	134,703	17,479	87.0%	85.3%	-1.70%
C. Other Division A (4% COLA)	42,560	48,751	6,191	83.9%	81.9%	-2.00%
D. Salt Lake City	84,679	89,915	5,236	73.1%	71.9%	-1.20%
E. Ogden	17,879	18,833	954	75.1%	74.1%	-1.00%
F. Provo	12,469	13,453	984	76.7%	75.4%	-1.30%
G. Logan	6,258	6,792	534	79.2%	77.8%	-1.40%
H. Bountiful	6,323	6,531	208	73.1%	72.5%	-0.60%
I. Other Division B (2.5% COLA)	52,569	58,793	6,224	81.7%	80.0%	-1.70%
J. Other Division B (4% COLA)	5,578	6,292	714	85.5%	83.9%	-1.60%
V. Firefighters						
A. Division A	(195)	2,129	2,324	100.1%	98.7%	-1.40%
B. Division B	18,035	27,810	9,774	97.9%	96.7%	-1.20%
VI. Judges	35,489	35,489	0	81.6%	81.6%	0.00%
V. Tier II - Hybrid Plans ²						
A. Public Employees	(7,119)	(6,756)	364	108.7%	108.2%	-0.50%
B. Public Safety and Firefighter	(1,234)	(943)	291	116.6%	112.2%	-4.40%
IV. Grand Total	\$ 4,027,125	\$ 4,250,543	\$ 223,418	85.5%	84.8%	-0.70%