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FISCAL IMPACT STATEMENT

LS 6997

BILL NUMBER: HB 1205

NOTE PREPARED: Feb 22, 2010

BILL AMENDED: Feb 22, 2010

SUBJECT: Pensions.

FIRST AUTHOR: Rep. Niezgodski

FIRST SPONSOR: Sen. Kenley

BILL STATUS: 2nd Reading - 2nd House

**FUNDS AFFECTED: X
X**

**GENERAL
DEDICATED
FEDERAL**

IMPACT: State & Local

Summary of Legislation: (Amended) *Deferred Compensation for State Employees*- The bill provides that if an employee does not choose another amount, the state shall deduct from the employee's compensation the greater of: (1) the maximum amount of any match provided by the state on behalf of the employee to a state deferred compensation plan; or (2) \$15; and deposit the amount deducted into the employee's account in the plan.

Indiana Public Retirement System- This bill establishes the Indiana Public Retirement System (System) to administer and manage the following:

(1) PERF. (2) TRF. (3) The Judges' Retirement Fund. (4) The Prosecuting Attorneys Retirement Fund. (5) The State Excise Police, Gaming Agent, Gaming Control Officer, and Conservation Enforcement Officers' Retirement Fund. (6) The 1977 Police Officers' and Firefighters' Pension and Disability Fund. (7) The Legislators' Retirement System. (8) the Pension Relief Fund. (9) the Special Death Benefit Fund. (10) The State Employees' Death Benefit Fund.

The bill also creates an 11-member board of trustees for the System (Board) consisting of 10 members appointed by the Governor and the Director of the Budget Agency (or designee) serving as an ex officio voting member; requires a trustee to complete annually at least 12 hours of trustee education; provides that the Board's powers and duties are the combined powers and duties of the PERF and TRF boards; provides that each retirement fund continues as a separate fund managed by the Board; provides for a director of the system who is appointed by and serves at the pleasure of the Board; requires the director to employ managers for PERF and TRF; and (17) allows the director to employ managers for one or more of the other public retirement funds of the system.

Thirteenth Check Provision- The bill also provides for a thirteenth check for PERF and TRF members, survivors, and beneficiaries; provides for a thirteenth check for employee beneficiaries of the State Police

1987 Benefit System who retired or were disabled after June 30, 1987, and before July 2, 2008, and were entitled to receive a monthly benefit as of June 1, 2010; and repeals provisions that establish the PERF and TRF boards.

Effective Date: Upon passage; May 1, 2010; July 1, 2010.

Explanation of State Expenditures: (Revised) *Deferred Compensation for State Employees-* The State Auditor's office will need to make minor changes to its payroll system in order to implement the changes in payroll deduction. The bill's requirements are within the agency's routine administrative functions and should be able to be implemented with no additional appropriations, assuming near customary agency staffing and resource levels.

The bill changes the initial automatic deduction amounts for the deferred compensation plans for new state employees. The change will not affect state expenditures.

Current statute provides that an amount equal to the administratively determined state matching contribution will be deducted unless the employee chooses a different amount. The bill changes the automatic initial employee deduction amount to be equal to the greater of (1) the administratively determined state match or (2) \$15 per pay period. Prior to CY 2010, the state match had been \$15 per pay period. However, the Governor announced in December 2009 that the state match will be suspended beginning January 1, 2010. Consequently, the automatic initial employee deduction amount will remain at \$15 unless the employee chooses a different amount, the same as under current statute.

Indiana Public Retirement System- The total impact of this provision on the PERF and TRF pension funds will depend on complete implementation and the extent to which economies are achieved, both in lowering administrative and investment costs, along with generating higher investment returns. A consulting firm retained by PERF and TRF estimated a one-time administrative cost savings of \$8.9 M and recurring annual savings of \$1.4 M with combining the administration of the funds. The bill also eliminates one executive director position and reduces the number of overall trustees.

Savings generated from this provision will not directly translate to any near-term reductions in state or local expenditures for member benefits. This provision directly affects PERF and TRF administrative costs, which would result in savings to the pension funds over a long period of time. Other things being equal, such as earnings on assets and member experience, an increase in administrative savings could ultimately affect the contribution rates by the members' employers, which at the state level would come from appropriations made by the state General Fund and dedicated funds.

Thirteenth Check Provision- The bill also provides a one-time 13th check to eligible PERF and TRF members, payable not later than October 1, 2010, and to members of the State Police 1987 Benefit System, payable not later than July 1, 2010. The state is impacted because it is an employer of PERF members and State Police 1987 Benefit System members, and the payor of pension benefits under the TRF Pre-1996 Account. The additional benefit provisions provided in this bill will result in an increase in the unfunded accrued pension liability for the state as an employer and payor of pension benefits beginning in FY 2011 and years thereafter.

A summary of the costs of this provision on the state for the three pension funds is provided in the following table.

Summary of Cost Impact on the State from 13th Check.				
	PERF	TRF (Pre-1996)	State Police	Total Impact
Change in Unfunded Accrued Liability	\$7.56 M	\$15.3 M	\$0.127 M	\$22.99 M
Change in Annual Funding *	\$0.580 M		\$9,200	\$0.589 M
Change in Annual Funding as % of Pay	0.034%		0.013%	
* The costs of providing the benefit adjustments provided in this bill do not directly or immediately translate into changes in contribution rates. Benefit changes, unfunded accrued liability, earnings on fund assets, and experience gains or losses will be accounted for in the July 1, 2010, valuation, which will be used to determine contribution levels beginning July 1, 2011 (i.e., FY 2012).				

[Estimates for the impacts are based on the actuarial funding methods and assumptions used in the July 1, 2009, valuations.]

Additional Details-

PERF 13th Check: There is no provision in current statute for a 13th check. The PERF Fund is actuarially funded by employer contributions and earnings from fund assets. The level of PERF employer contributions is established by the PERF Board. Considering this 13th check benefit adjustment only, the associated state contribution level should be sufficient to fund the benefit for retired state employee PERF members. The funds affected for the annual funding for PERF contributions across all state agencies are the state General Fund (about 55% of the total) and various dedicated funds (about 45% of the total). The one-time payment of the 13th check will be made in FY 2011.

TRF (Pre-1996 Account) 13th Check: The TRF Fund consists of two accounts: the Pre-1996 Account and the 1996 Account. The Pre-1996 Account is funded by the state, and the 1996 Account is funded primarily by local school corporations. The one-time payment of the 13th check will be made in FY 2011. The impact to the state for the Pre-1996 Account is shown in the summary table, above. [The impact for the 1996 Account is shown in the *Explanation of Local Expenditures*, below.]

The Pre-1996 Account is not actuarially funded, but rather is funded on a pay-as-you-go basis by state General Fund appropriations, investment earnings of fund assets, and, if necessary, additional amounts obtained from the Pension Stabilization Fund. For the TRF Pre-1996 Account contributions, the state General Fund contribution level is specified in statute.

State Police 13th Check: There is no provision in current statute for a 13th check for members of the State Police 1987 Benefit System. The cost to the state for a 13th check for the State Police is shown in the table, above. The State Police System is funded by appropriations, half from the state General Fund and half from the Motor Vehicle Highway Account. (The funded status would remain at 78.5%.) It is estimated that there would be 470 employee beneficiaries eligible for the 13th check and that the 13th check would equal approximately \$269 per beneficiary.

Background - Indiana Public Retirement System: The following table shows the administrative and investment expenses for PERF and TRF for FY 2009.

FY 2009 Expenses	PERF	TRF
Administrative	\$26.06 M	\$8.07M
Investment	\$63.77 M	\$31.87 M
Total	\$89.83 M	\$39.94 M

Explanation of State Revenues: *Indiana Public Retirement System:* The pooling of assets also could generate higher investment returns and lower investment costs for the pension funds. PERF and TRF estimate that the pooling of assets could generate an increase of 0.2% in investment return. As of November 30, 2009, PERF net assets amounted to \$14.2 B, and TRF net assets were \$8.1 B. Combined net assets totaled \$22.3 B. The 0.2% increase in investment return is equivalent to approximately \$44.6 M in incremental annual investment returns.

Increased investment returns generated from this provision will not directly translate to any near-term reductions in state or local expenditures for member benefits. However, this provision could result in additional earnings to the pension funds over a longer period of time. Other things being equal, such as member experience, an increase in earnings could ultimately affect the contribution rates by the members' employers.

Explanation of Local Expenditures: *Indiana Public Retirement System-* The bill may also provide some administrative efficiencies to local employers. PERF and TRF have estimated an additional annual savings of \$100,000 for lower employer administrative costs.

PERF 13th Check- There is no provision in current statute for a 13th check. The cost of a 13th check to local units and school corporations for PERF members is provided in the following table.

13th Check	PERF-Local
Change in Unfunded Accrued Liability	\$11.28 M
Change in Annual Funding *	\$870,000
Change in Annual Funding as % of Pay	0.028%
* The costs of providing the benefit adjustments provided in this bill do not directly or immediately translate into changes in contribution rates. Benefit changes, unfunded accrued liability, earnings on fund assets, and experience gains or losses will be accounted for in the July 1, 2010, valuation, which will be used to determine employer contribution levels beginning January 1, 2012.	

The level of PERF employer contributions is established by the PERF Board. Considering this 13th check benefit adjustment only, the associated contribution level should be sufficient to fund the benefit for retired PERF members.

TRF (1996 Account) 13th Check- The 1996 Account is prefunded, with an actuarially calculated contribution equal to the benefit accrual cost for the year (the plan's normal cost) plus a 30-year amortization of the unfunded accrued benefit liability. The impact is summarized in the following table.

Impact on School Corporations as Employers (TRF 1996 Account) *	
	13th Check
Change in Unfunded Accrued Liability	\$0.70 M
Change in Annual Funding	\$0.05 M
Change in Annual Funding as % of Pay	< 0.01%
* Noncertificated employees of school corporations are members of PERF and for which the impact would be included in the table for local units.	

Account revenues include annual contributions from school corporations at a percentage of payroll, currently 7.50%, and investment earnings on fund assets. Considering this 13th check benefit adjustment only, the associated contribution level should be sufficient to fund the 13th check for retired TRF 1996 Account members.

Explanation of Local Revenues:

State Agencies Affected: All

Local Agencies Affected: Those units with members in PERF and school corporations with members in PERF and TRF.

Information Sources: Doug Todd of McCready & Keene, Inc., actuaries for PERF, 317-576-1508; John Dowell, Nyhart Group, actuaries for TRF, 317-845-3580; Terren Magid, Executive Director, PERF, 317-234-4375; Steve Barley, Deputy Director and Chief Operating Officer, PERF, 317-233-4184; Steve Russo, Executive Director, TRF, 317-232-3864; Brent Plunkett, Payroll Director, State Auditor’s office, 317-232-3299.

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DEFINITIONS

Cost-of-Living Adjustment- An across-the-board increase (or decrease) in wages or pension benefits according to the rise (or fall) in the cost of living as measured by some index, often the Consumer Price Index (CPI).

Present Value– The present value (sometimes called actuarial present value) of an amount or series of amounts payable or receivable in the future is their current worth after discounting each such amount at an assumed rate of interest and adjusting for the probability of its payment or receipt.

Thirteenth Check– A thirteenth check is an annual supplemental retirement allowance arising from earnings on the investments of a system in excess of those determined as needed for other purposes. Unlike a cost-of-living adjustment, the amount of this supplemental retirement allowance does not increase the pension base.

Unfunded Actuarial Liability -The actuarial liability, sometimes called the unfunded liability, of a retirement system at any time is the excess of its actuarial liability at that time over the value of its cash and investments.