Testimony – In Support
House Bill No. 116
Introduced by Rep. Pat Ingraham
By Request of the Teachers' Retirement System

Exhibit No. 10
3-16-2011
HB 116

Senate State Administration
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By now, most everybody in America has seen and read media exposés describing the financial problems of state and local pension funds. We all agree that the pension fund deficit caused by the 2008 and 2009 decline in the market value of retirement assets must be addressed; the question is, how and when? The good news is that the Teachers' Retirement System (TRS) is not going to run out of money in the next two, 10 or 15 years. While we have time to address the problem, we need to get started now.

House Bill 116 includes several amendments that would strengthen "actuarial controls" where weaknesses have been found, which can have an adverse impact on funding. These are actuarial factors or controls based on actuarial determinations that are codified in statute. HB 116 will strengthen these actuarial controls to avoid future losses and/or overpayment of retirement benefits.

Sections 1 & 10 – Working Retiree Controls:

- Establishing employer liability regarding reports relating to retired members
  - Employers who do not timely and correctly report could be held jointly and severally liable with the retired member for any repayment due TRS.
- Amending provisions governing retirees returning to work in a TRS eligible position
  - Discontinue consideration of employment status for retirees returning to work in a TRS eligible position (part-time or full-time service), leaving only the one-third compensation limitation for working retirees.
  - If a retiree is employed under the one-third earnings limit in a TRS-reportable position and is concurrently employed by the same employer in a position that, on its own, would not be a TRS-reportable position, the positions and compensation would be deemed to be combined as a single TRS-reportable position.

Sections 2 through 8 – Effective July 1, 2012, Charge the Actuarial Interest Rate on all Service Purchases:

- Changing the actuarial interest rate on all service purchase agreements initiated on or after July 1, 2012
  - For members hired prior to July 1, 1989, current law limits the rate of interest charged on service purchase agreements to the rate credited to the member's account. With the

current rate credited to member's accounts at only 0.25%, these service purchases are significantly underfunded. Therefore, all sections of current law governing service purchase agreements are amended to charge the actuarial assumed rate (currently 7.75%). This change would only affect purchase agreements that are effective after July 1, 2012. Members hired after July 1, 1989, are currently required to pay the full actuarial cost for most service purchases.

Section 9 – 10% Cap Exemptions:

- Revising caps on compensation that can be used in the calculation of average final compensation
  - Eliminate all exceptions to the 10% cap, except for an increase that results from movement on an employer adopted salary matrix.

Section 11 – Full Actuarial Reduction for Early Retirement:

- Updates the current actuarial factors for early retirement
  - Members electing to retire early (less than 25 years of service or less than age 60) receive a reduced "early" retirement benefit. The reduction is 0.5% for the first 60 months early and 0.3% for each additional month. The maximum reduction is 48.0%. The Actuaries recommend Early Retirement Factors should be true actuarially equivalent factors so that the system does not subsidize early retirement for the member. The following examples show how benefits would be affected by the proposed change.

Early Retirement Factors, Current & Proposed

Age At Retirement	5 Years of Service		10 Years of Service		15 Years of Service		20 Years of Service	
	Current	Proposed	Current	Proposed	Current	Proposed	Current	Proposed
50	0.5200	0.4080	0.5200	0.4080	0.5200	0.4080	0.7000	0.6312
55	0.7000	0.6312	0.7000	0.6312	0.7000	0.6312	0.7000	0.6312
58	0.8800	0.8291	0.8800	0.8291	0.8800	0.8291	0.8800	0.8291
59	0.9400	0.9100	0.9400	0.9100	0.9400	0.9100	0.9400	0.9100
60	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000

Actuarial Required Contributions (ARC)

While HB 116 moves us in the direction of actuarially funding TRS, it does not immediately increase contributions to the degree that would be necessary to meet the Actuarially Required Contribution (ARC) rate in the next biennium. The actuaries have estimated that the ARC would need to increase by 2.20% effective July 1, 2011, and by another 2.02% effective July 1, 2012, for a total of 4.22% over the next biennium. If we cannot begin to fund the ARC now, the required rate increase most likely will continue to grow, thus increasing the size of the problem the next Legislature will have to address. In addition, failure to contribute the ARC could have an adverse impact on the State's credit rating; although, I believe if the legislature starts to address the problem now it is far less likely the State's credit rating would be affected. This belief is supported by a recent press release from Fitch:

"The analysis of long-term obligations, including pensions, is an important part of Fitch's rating review for state and local government credits. Fitch has downgraded a number of credits due in part to pension funding issues, and will continue to take such action as warranted…."

"However, since governments and their tax bases are long-term in nature, officials in most cases have some time to fully implement changes to control their long-term liabilities. Similarly, the beneficial impact of any adjustments on funding levels and contributions will accrue over an extended period."

"Although a pressing need remains to set many pension systems on a more sustainable footing, what Fitch has observed over a long period of time is generally responsible financial management actions by state and local governments, and Fitch believes officials will work in the near term to improve funded ratios."

Fiscal Note

Reduces UAAL $6.8 million
Reduces amortization period 2.3 years