

BILL # HB 2558

TITLE: retirees; health insurance; enhanced subsidies

SPONSOR: Carruthers

STATUS: As amended by the House Retirement and Government Operations Committee

REQUESTED BY: House

PREPARED BY: Timothy Sweeney

FISCAL YEAR

	2002	2003	2004
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EXPENDITURES

General Fund	\$-0-	\$-0-	\$185,200
Other Appropriated Funds	<u>-0-</u>	<u>-0-</u>	<u>61,900</u>
Total	\$-0-	\$-0-	\$247,100

FISCAL ANALYSIS

Description

HB 2558 extends the temporary retiree health insurance subsidies enacted in the 2001 Legislative Session through June 30, 2004. Currently, these temporary subsidies are set to expire on June 30, 2003, and apply to members of the Arizona State Retirement System (ASRS), the Public Safety Personnel Retirement System (PSPRS), the Corrections Officer Retirement Plan (CORP), and the Elected Official Retirement Plan (EORP).

In addition to the provisions of the original bill, HB 2558 was amended by the House Retirement and Government Operations Committee (RGO) to extend the added “non-service area” subsidy to out-of-state retirees. Currently, retirees in non-service areas receive a higher health insurance subsidy due to higher health insurance costs in rural areas. The amendment offered by RGO extends the definition of non-service area (which currently only includes in-state retirees) to include out-of-state retirees.

Estimated Impact

Contribution rates for ASRS, PSPRS, CORP, and EORP have already been set for FY 2002 and FY 2003, therefore there will be no fiscal impact for these two years. The Retirement systems’ actuaries estimate that HB 2558 as amended would increase ASRS contribution rates by 1.1 basis points (.011%), PSPRS rates by 5.5 basis points (.055%), CORP rates by 1.2 basis points (.012%), and EORP rates by 8.6 basis points (.086%) above current levels in FY 2004. These increases in the contribution rates will result in increased Employee Related Expenditures (ERE) for agencies in FY 2004. The table below details the ERE increase and the associated General Fund and Other Appropriated Funds impact. Employee contribution rates are fixed in PSPRS, CORP, and EORP; therefore, this bill would only impact employer contributions. In ASRS, however, this increase applies to both the employer and employee contribution rates.

<u>Retirement System</u>	<u>Additional % of Employee’s Salaries Contributed</u>	<u>General Fund Impact</u>	<u>Other Appropriated Funds Impact</u>
ASRS	.011%	\$115,000	\$39,800
PSPRS	.055%	18,500	21,900
CORP	.012%	38,300	200
EORP	.086%	<u>13,400</u>	<u>-0-</u>
Total		\$185,200	\$61,900

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Estimated Impact (Continued)

The total estimated impact in FY 2004 for the four retirement systems is approximately \$185,200 from the General Fund and \$61,900 from Other Appropriated Funds.

Assumptions

The table below displays the current subsidies received by all retirees, and the additional amount received by retirees in rural areas. The subsidy amounts received vary depending on whether the retiree has one or more dependants, and whether the retiree and/or the dependants are eligible for Medicare.

	<u>Regular Subsidy for all Retirees</u>	<u>Special Subsidy for Rural Retirees</u>
No Dependant, has Medicare	\$100	\$170
No Dependant, no Medicare	\$150	\$300
With Dependant(s), and Medicare	\$170	\$350
With Dependant(s), no Medicare	\$260	\$600

Provisions Resulting in an Increased Contribution Rate

According to actuaries contracted by the retirement systems, the provisions in HB 2558 that extend the temporary subsidy for an additional year would result in a 1 basis point increase for ASRS, a 4.5 basis point increase for PSPRS, a 1 basis point increase for CORP, and a 7 basis point increase for EORP.

Actuaries report that the provisions included in the RGO amendment that extends the temporary subsidy to out-of-state retirees would result in a 0.1 basis point increase for ASRS, a 1 basis point increase for PSPRS, a 0.2 basis point increase for CORP, and a 1.6 basis point increase for EORP.

System Specific Assumptions

ASRS

ASRS assets exceed liabilities by \$2.6 billion. These monies are used to reduce the total contribution (*which is the amount required to achieve actuarial soundness*) from current employers by lowering the employer contribution rate from 5.36% to 2.0% of employee's salaries. Therefore, benefit enhancements have a corresponding cost impact if they cause the contribution rate to increase. When the actual ASRS contribution rate is below the statutorily established floor of 2%, it is possible to enact benefit enhancements without having an impact to the General Fund (*provided that they do not raise the contribution rate above the 2% floor*). While the ASRS contribution rate for the FY 2002-FY 2003 biennium is 2.0%, if the rate were to be adjusted to reflect fund performance and benefit enhancements enacted in the 2001 Legislative Session, the actual contribution rate would be 3.86%. Though, due to the fact that the new contribution rates are established on a biennial basis, in FY 2002 employers and employees are contributing 2.0%, which is less than the actuarially required amount of 3.86%. Therefore, according to current actuarial projections, there is no "cushion" to reduce the 1.1 basis point increase.

When a benefit enhancement is permanent there is a cost component associated with providing the benefit to future years of service. Because this is a temporary benefit, this component does not apply. However, extending the temporary health insurance subsidy for another year and expanding it to out-of-state retirees provides a benefit that was not previously incorporated into the contribution rate paid by current members receiving the benefit; therefore, when enacted it increases liabilities by \$11.6 million, as determined by the actuary. This amount is recovered over 17 years through the contribution rate. The total impact of this bill as amended (1.1 basis points) represents the portion to fund this liability for existing years of service.

From an actuarial perspective, this increased liability of \$11.6 million will reduce the \$2.6 billion in "excess" assets.

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Assumptions (Continued)

System Specific Assumptions

PSPRS

PSPRS assets exceed liabilities by \$987.2 million. These monies are used to reduce the total contribution (*which is the amount required to achieve actuarial soundness*) from current employers by lowering the employer contribution rate from a systemwide average of 11.21% to 3.75% of employee's salaries. Therefore, benefit enhancements have a corresponding cost impact if they cause the contribution rate to increase. When the actual PSPRS systemwide average contribution rate is below the statutorily established floor of 2%, it is possible to enact benefit enhancements without having an impact to the General Fund (*provided that they do not raise the contribution rate above the 2% floor*). The systemwide average rate for the FY 2002-FY 2003 biennium is 4.21%, because the contribution rate is set on a biennial basis. However, if the rate were to be adjusted in FY 2003 to reflect fund performance and benefit enhancements enacted in the 2001 Legislative Session, the actual systemwide average rate would be 3.75%. Therefore, according to current actuarial projections for most PSPRS participants, there is no "cushion" to reduce the 5.5 basis point increase. Because the average actual biennial contribution rate is higher than the average required rate for FY 2003, PSPRS FY 2003 collections may exceed the amount required for actuarial soundness, on average. Therefore, the actual contribution rate increase in FY 2004 may be slightly smaller than currently projected.

When a benefit enhancement is permanent there is a cost component associated with providing the benefit to future years of service. Because this is a temporary benefit, this component does not apply. However, extending the temporary health insurance subsidy for another year and expanding it to out-of-state retirees provides a benefit that was not previously incorporated into the contribution rate paid by current members receiving the benefit; therefore, when enacted it increases liabilities by \$6.7 million, as determined by the actuary. This amount is recovered over 20 years through the contribution rate. The total impact of this bill as amended (5.5 basis points) represents the portion to fund this liability for existing years of service.

From an actuarial perspective, this increased liability of \$6.7 million will reduce the \$987.2 million in "excess" assets.

The PSPRS discussion above is based upon the systemwide average contribution rate for PSPRS employers, which facilitates a general understanding of the bill's impact. In addition, the actuarial analysis of a benefit enhancement is in terms of the impact on the systemwide average. It is important to note, however, that in PSPRS each participating employer does not contribute the systemwide average; but instead contributes an actuarially determined amount specific to each employer.

The largest PSPRS General Fund employer is the Department of Public Safety (DPS). Currently, the actuarially determined PSPRS contribution rate for DPS is 0%. The state, however, is required to pay the 2% floor. Therefore, benefit enhancements that total 200 basis points or less could potentially be enacted without impacting the DPS budget in FY 2004. Of the other state participants in PSPRS, only NAU Police and ASU Police have contribution rates that fall below the 2% floor. Other state participants, however, such as Capitol Police and U of A Police have contribution rates above the 2% floor. Thus, for these agencies, any benefit enhancements will result in a cost increase in their FY 2004 budget.

Additionally, it should be noted that DPS officer pensions are funded out of the Highway Patrol Fund, with the remaining monies from this fund used by DPS for general expenditures. DPS, however, currently expends the maximum amount of Highway Patrol Funds. Historically, an increase in the retirement contribution rate leads to a corresponding reduction in the amount of Highway Patrol Fund monies available for general expenditure. This decrease must then be covered by General Fund monies. Thus, even though DPS officer pensions are directly funded from the Highway Patrol Fund, an increase in the contribution rates may have a corresponding impact on the General Fund. For this reason, the cost of this increase has been included in the General Fund estimated impact. Though as mentioned, due to the 2% floor for DPS contributions, the system may be able to absorb the impact of this benefit increase depending on the total package of PSPRS benefit enhancements enacted during the 2002 Legislative Session.

CORP

CORP assets exceed liabilities by \$221.8 million. These monies are used to reduce the total contribution (*which is the amount required to achieve actuarial soundness*) from current employers by lowering the employer contribution rate from a

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Assumptions (Continued)

System Specific Assumptions

CORP

systemwide average of 5.79% to 1.71% of employee's salaries. Therefore, benefit enhancements have a corresponding cost impact if they cause the contribution rate to increase. When the actual CORP systemwide average contribution rate is below the statutorily established floor of 2%, it is possible to enact benefit enhancements without having an impact to the General Fund (*provided that they do not raise the contribution rate above the 2% floor*). Without the 2% floor, the systemwide average rate for the FY 2002-FY 2003 biennium would have been 1.15%, because the contribution rate is set on a biennial basis. However, if the rate were to be adjusted in FY 2003 to reflect fund performance and benefit enhancements enacted in the 2001 Legislative Session, the actual systemwide average rate would be 1.71%. Therefore, according to current actuarial projections, only benefit enhancements that total 29 basis points or less could potentially be enacted without having an CORP impact to the General Fund in FY 2004. This 29 basis point "cushion" could be available to reduce the 1.2 basis point impact of this benefit enhancement, depending on the total package of CORP retirement changes enacted during the 2002 Legislative Session.

When a benefit enhancement is permanent there is a cost component associated with providing the benefit to future years of service. Because this is a temporary benefit, this component does not apply. However, extending the temporary health insurance subsidy for another year and expanding it to out-of-state retirees provides a benefit that was not previously incorporated into the contribution rate paid by current members receiving the benefit; therefore when enacted it increases liabilities by \$0.8 million, as determined by the actuary. This amount is recovered over 20 years through the contribution rate. The total impact of this bill as amended (1.2 basis points) represents the portion to fund this liability for existing years of service.

From an actuarial perspective, this increased liability of \$0.8 million will reduce the \$221.8 million in "excess" assets.

The CORP discussion above is based upon the systemwide average contribution rate for CORP employers, which facilitates a general understanding of the bill's impact. In addition, the actuarial analysis of a benefit enhancement is in terms of the impact on the systemwide average. It is important to note, however, that in CORP each participating employer does not contribute the systemwide average; but instead contributes an actuarially determined amount specific to each employer. The largest CORP General Fund employer is the Arizona Department of Corrections (ADC). Currently, the actuarially determined CORP contribution rate for ADC is 1.72%, which is only slightly higher than the systemwide average. Therefore, only benefit enhancements that total 28 basis points or less could potentially be enacted without impacting the ADC budget in FY 2004. In comparison, however, the Arizona Department of Juvenile Correction's (DJC) actuarially determined contribution rate specific to the agency is 3.26%, which is above the 2.0% floor. Therefore, any benefit enhancements enacted will result in a General Fund cost increase in the DJC budget in FY 2004.

EORP

EORP assets exceed liabilities by \$104.8 million. These monies are used to reduce the total amount of court fees needed to cover employer contributions from an average of 21.0% to 7.55% of employee's salaries. It is important to note that the entire cost for EORP employer contributions are currently funded by court fees. EORP receives a fixed percentage of court fees to fund employer contributions, and in previous years these court fees have been large enough to produce a buffer. If, however, court fees were not enough to cover the employer's contributions, General Fund monies would be needed. Prior to the 2001 Legislative Session this buffer was between 1.5% and 2% (150 to 200 basis points). However, the total package of benefit enhancements passed in the 2001 Legislative Session has eliminated this buffer and the total cost impact of the contribution rate increase associated with this bill is included in the General Fund impact.

When a benefit enhancement is permanent there is a cost component associated with providing the benefit to future years of service. Because this is a temporary benefit, this component does not apply. However, extending the temporary health insurance subsidy for another year and expanding it to include out-of-state retirees provides a benefit that was not previously incorporated into the contribution rate paid by current members receiving the benefit; therefore, when enacted it increases liabilities by \$0.7 million, as determined by the actuary. This amount is recovered over 20 years through the contribution rate. The total impact of this bill as amended (8.6 basis points) represents the portion to fund this liability for existing years of service.

From an actuarial perspective, this increased liability of \$0.7 million will reduce the \$104.8 million in "excess" assets.

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Local Government Impact

The changes proposed by HB 2558 as amended would result in an estimated FY 2004 local government and non-appropriated fund impact of approximately \$1.3 million. Prior to the RGO amendment, JLBC estimated the FY 2004 local government and non-appropriated fund impact of HB 2558 to be approximately \$1.1 million.

Amendments

HB 2558 was amended by RGO to extend the temporary health insurance subsidies for retirees in “non-service” areas to include out-of-state retirees.

Prior to the RGO amendment, the JLBC Staff estimated the impact of HB 2558 in FY 2004 to be approximately \$159,700 from the General Fund, and \$53,300 from Other Appropriated Funds. Therefore, the amendment increases the estimated impact by \$25,500 from the General Fund and \$8,600 from Other Appropriated Funds.

4/04/02