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House Bill 1198

Actuarial Cost Study prepared for
Joint Committee on Public Retirement and Social Security Programs
of the Arkansas 89th General Assembly

Provisions of the Bill

House Bill 1198 affects the Arkansas Teacher Retirement System (ATRS).

House Bill 1198 allows the ATRS Board of Trustees to create a Tier II Benefit plan for members hired on or after July 1, 2015. In general, the Tier II plan must afford members the same benefits and rights as current ATRS members. However, House Bill 1198 explicitly states that the Tier II plan may modify: age requirements for unreduced benefits, years of service requirements for unreduced benefits, qualifications and benefit reductions for early retirement, multipliers for service, years of service credit required for vesting, lump sum death benefits, monthly stipend amounts, survivor benefits, disability benefits, cost-of-living adjustments, and the Teacher Deferred Retirement Option Plan.

The limitations provided in the bill are:

- The age requirement for unreduced benefits shall not exceed age 67.
- The years of service requirement for unreduced benefits shall not exceed 35 years.
- A member shall be eligible for early retirement after 25 years of service.
- The multiplier for contributory service shall be between 1.75% and 2.15%, and the multiplier for non-contributory shall be between 0.5% and 1.39%.
- Service required to vest shall not exceed 10 years.
- The lump sum death benefit shall not exceed $10,000.
- A monthly stipend shall not exceed $75.
- The survivor benefits shall not exceed 20% of a member's highest one-year salary per survivor, or 60% in total.
- Disability benefits shall not exceed the benefits payable as if the member retired under age and service retirement.
- A simple cost-of-living adjustment (COLA) may be provided, but it may be adjusted, tied to an inflation index, or applied to a future year. It shall not exceed 3%.

House Bills 1194 and 1198 both allow the ATRS Board to make similar changes to the benefit multiplier. House Bill 1194 has the potential to affect all current and future retirees, whereas House Bill 1198 would only affect new hires.

Fiscal Impact

The ultimate effect of House Bill 1198 will depend on the extent to which the ATRS decides to implement its menu of possible changes. If all of the options laid out in House Bill 1198 are fully implemented then the Tier II cost savings would eventually meet the current 2.80% of payroll shortfall. Since Tier II only makes the changes for new hires, it would take several years (usually about 10) to fully implement the savings that are created. In general, none of these changes would change the Unfunded Accrued Liabilities currently in place, only future normal costs. So the savings would be phased in as new members are hired. The table below shows an example of a 0.25% reduction in multipliers for new hires, resulting in 1.90% contributory and 1.14% non-contributory multipliers.

	6/30/2012 Valuation (14% ER Contrib.)	If House Bill 1198l Implemented .25% Mult. Decrease	Savings Fully (10 years) Implemented
Unfunded Actuarial Liability (millions)	$4,655	$4,655	$ 0
Gross Normal Cost (% of Pay)	11.73%	10.60%	1.13%
Average Member Contribution	4.80%	4.80%	
Net Normal Cost	6.93%	5.80%	1.13%
Payoff UAL in 30 Years	9.87%	9.87%	
Needed Employer Rate	16.80%	15.67%	1.13%
Current Employer Rate	14.00%	14.00%	
Available to pay UAL	7.07%	8.20%	1.13%

The change illustrated by this example would not be sufficient to put the plan back on a 30 year amortization path by itself. This simple example assumes all other assumptions are met during the phase-in period. Without other changes or other gains, the UAL would grow during the phase-in period and the effect of this change would be diminished.

Policy Consideration

There are a total of six bills (SB123, SB130, SB162, HB1194, HB1198, HB1200) that give certain authority to the ATRS board to set benefits and contribution rates. Benefits and contribution rates have historically been set by the legislature, and the ATRS board adopts policy to implement them. This would be a change to that practice.

Other

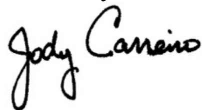
It would appear that the word "Retirement" was omitted from line 32 on page 2.

The committee should consider the risks associated with creating new tiers in retirement systems. A new tier does not eliminate any of the unfunded liability of a plan. Since this "closed" portion continues to age, it has the effect of having upward pressure on those liabilities. Also, if those liabilities are amortized over a 30 year, percent of pay, open period basis, as is currently used, then this could cause upward pressure on the payoff rates.

The contributory and non-contributory multipliers have been established over the years to reflect the difference in total contribution rates. In fact, in reviewing the total gross normal costs rates of the two groups the difference is currently a little more than 6%. House Bill 1194 allows for a much greater reduction in the non-contributory multiplier relative to the allowable reduction in the contributory multiplier. It is our opinion that if difference in normal costs grew too far from the 6% contribution rate, then assumptions would need to be added to measure the rate of non-contributory members becoming contributory. This would tend to lessen the cost savings described.

House Bills 1194 and 1198, along with Senate Bill 163 could all have overlapping effects depending on how they are implemented. That is, the change from one bill could impact the savings from another bill. This would mean that the effects of these three bills might not be able to be added together and produce the combined result. All three of these bills would also be affected by any change in final average salary that is allowed under current law and being considered by the ATRS board.

Sincerely,



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