

House Bill 1216

(As Engrossed February 9, 2015)

Actuarial Cost Study prepared for
Joint Committee on Public Retirement and Social Security Programs
of the Arkansas 90th General Assembly

Provisions of the Bill

House Bill 1216 affects the closed Local Firemen’s and Policemen’s Pension and Relief Funds (“Local Plans”).

Arkansas Code Annotated §24-11-807 and §24-11-416 provide language detailing when the proration of benefits is allowed for certain underfunded Local Plans covering firefighters and police officers. The language is slightly different for police and fire funds, but a standing Attorney General’s Opinion, No. 2005-041, suggests that proration of benefits is not allowed “unless the assets of the fund are insufficient to pay full benefits in the current fiscal year.” No other mechanism in current law allows for the boards of such funds to reduce benefits.

House Bill 1216 would add a new subsection which explicitly allows the board of trustees to prorate or reduce benefits to participants in funds which are determined “not to be actuarially sound or to be in substantial risk of ruin before all beneficiaries receive their lifetime benefits.”

Fiscal Impact

From an actuarial perspective, the financial standing of a plan would improve by utilizing a benefit reduction provided for in House Bill 1216—lower benefit levels require less assets to support. However, the purpose of these retirement plans is to provide promised benefits; any reduction would clearly be at odds with that purpose.

Based on the summary of the actuarial valuations as of December 31, 2013, 105 of the 164 plans (plans with both paid and volunteer members are counted as two for this purpose) were not actuarially sound. The Pension Review Board currently has six plans that have been declared “Projected Insolvent” plans, that is, assets are projected to be depleted in less than 10 years. The Board has also declared twenty Local Plans to be “At Risk” plans, or within 15 years of depletion. We would assume that the “substantial risk of ruin” language of House Bill 1216 would be interpreted similarly to the current definition of “Projected Insolvent.”

There could be some small fiscal savings to the state if plans were to reduce benefits. The state subsidizes the Local Plans through the allocation of certain premium tax revenues. Although the formula is complex, the amount of revenue allocated to the Local Plans is proportional to how well funded they are on a “base benefits” basis, and any remaining premium tax monies are returned to

state general revenues. If benefits are reduced, then the plan's funding status would be improved (relative to the same plan with unreduced benefits); over time, this would result in lower premium tax allocations to the plan and could result in increased returns to state general revenue, dependent upon other factors. We estimate that the fiscal impact to the state would be small.

Other

The section of code that is added by House Bill 1216 makes provision for both fire and police Local Plans. The proposed section is in Subchapter 8 which deals only with local fire funds. This section may be better suited for the end of Subchapters 2 or 3 which deal with both types of funds.

The issues involved here are addressed at some length in Attorney General Opinions No. 2005-041, No. 2009-049, and No. 2009-102. The Attorney General's Opinions did not purport that current law would allow any benefit decrease prior to the year assets were to be depleted, so the change proposed by House Bill 1216 could address that concern. The Attorney General also opined that Arkansas Constitution Article 2, Section 17 could be invoked if any reduction were allowed and implemented. These concerns would increase the risk of future litigation if House Bill 1216 were made into law.

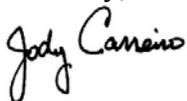
In light of the Attorney General's Opinions, the Committee may want to consider an amendment that any reduction not result in benefits below the minimum established elsewhere in law (generally, 50% of salary for paid members and \$100 per month for volunteers). Opinion No. 2009-049 further suggests that a reduction most likely to survive a legal challenge would be one which rolled back only those benefit increases which occurred after a member's retirement rights became vested. However, the opinion clearly states that "a judicial ruling may be necessary to definitively decide the matter."

Regarding similar provisions in the private sector, the Multiemployer Pension Reform Act of 2014 allows certain distressed multiemployer plans to enact benefit reductions in limited circumstances. Any benefit cuts in large plans are subject to a vote of affected workers and retirees.

House Bill 1216 does not address the possibility of a restoration of benefits after a Local Plan becomes actuarially sound. It is assumed that any restoration would have to be achieved through the benefit increase process in current law.

Please note that Osborn, Carreiro & Associates also serves as the actuaries for the Arkansas Fire and Police Pension Review Board.

Sincerely,



Jody Carreiro, EA, ASA, MAAA
Actuary