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FISCAL IMPACT REPORT

ORIGINAL DATE 2/23/09
 SPONSOR Saavedra LAST UPDATED 3/13/09 HB 854/aHAFC
 SHORT TITLE PERA Member & State Contribution Changes SB _____
 ANALYST Aubel/Moser

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

| | FY09 | FY10 | FY11 | 3 Year Total Cost | Recurring or Non-Rec | Fund Affected |
|----------------|------|--------------|--------------|-------------------|----------------------|-------------------|
| Original Bill* | | (\$42,600.0) | (\$42,600.0) | (\$85,200.0) | Nonrecurring | General Fund |
| HAFC Amendment | | (\$40,345.0) | (\$40,345.0) | (\$80,690.0) | Nonrecurring | General Fund |
| | | \$0.1 | \$0.1 | \$0.1 | Nonrecurring | PERA/ERB/Agencies |

(Parenthesis () Indicate Expenditure Decreases)

*Based on Legislative Finance Committee 2008 Post-Session Review: Compensation Appropriations – Appendix AA

ACTUARIAL IMPACT**

| Estimated Revenue | | | Recurring or Non-Rec | Fund Affected |
|-------------------|------------|------------|----------------------|----------------|
| FY09 | FY10 | FY11 | | |
| | (\$450.0)* | (\$450.0)* | N/A | PERA, JRA, MRA |
| | (Minimal)* | (Minimal)* | N/A | ERB |

(Parenthesis () Indicate Revenue Decreases)

**Estimated.

Companion to the General Appropriation Act (House Bill 2)

Relates to or conflicts with HJM 45, HB 79, HB 236, HB 246, HB 271 and companion HB 355, HB 351 and duplicate SB 366, HB 353, HB 453, HB 573, HB 616, HB 631, HB 648, HB 683, HB 684, HB 721, HB 731, HB 765, HB 798, SB 145, SB 231, SB 261, SB 428, SB 476, and SB 499

SOURCES OF INFORMATION

LFC Files

Responses Received From

Educational Retirement Board (ERB)
Public Employees Retirement Association (PERA)
State Personnel Office (SPO)
Corrections Department (CD)
New Mexico Higher Education Department (HED)
Public Defender Office (PDO)

No Response From

Public Education Department (PED)
Administrative Office of the Courts (AOC) (Responded after FIR produced.)

SUMMARY

Synopsis of HAFC Amendment

The House Appropriations and Finance Committee Amendment to House Bill 854 limits the 1.5 percent employer-employer pension contribution exchange to those with salaries over \$20 thousand.

FISCAL IMPLICATIONS

The fiscal impact of the HAFC amendment reduces the savings in general fund by approximately \$2.3 million. Other bills currently being considered may offset this savings reduction (see Conflicts, Duplications, Companionship, Relationship). Vacancy savings throughout FY10 are also expected to contribute to an offset of this savings reduction.

PERA also makes an additional comment on the impact to fund solvency:

If the total contributions are kept the same, but some of the contributions are shifted from employer to employee, the amortization period for that plan will increase. For the most part, the increase should be small. However, the more poorly funded a group is, the bigger the impact will be (such as in the Judicial Fund). In addition, the closer the normal cost is to the total contributions coming in, the greater the impact will be (such as in the Magistrate Fund). Based on the 95:100 employee-employer contribution ratio provided by PERA's actuaries, the estimated impact to the overall PERA plan is less than \$1 million for the two-year period.

ERB's actuaries indicated a minimal effect stemming from the contribution swap due to the stability of the employee base that does not lead to substantial refunds.

SIGNIFICANT ISSUES

ERB points out that overtime and other intermittent events may switch an employee in and out of the exemption during various pay periods, and ERB or PERA won't know what the actual annual salary will be until the end of the fiscal year. This would lead to administrative issues regarding overpayments or underpayments and reconciling employer-employee contributions. Internal Revenue Service rules may make this issue even more complicated.

The amendment also creates a “cliff effect” for those making \$20,000-\$20,330, which could potentially result in salary compression and less take-home pay for those employees than those making less than \$20,000 that are subject to the exemption.

The amendment also raises uncertainty regarding Legislative intent of the “\$20,000 and below” exemption. As currently worded, the amendment’s exemption provision would apply to both full-time equivalents making \$9.579 or less per hour and any employee earning any hourly wage with an annual salary of \$20,000 or less. This would include, for example, someone making \$35 per hour as a part time counselor in a school. SPO notes that of the 20,188 non-temporary classified employees, 467 earn \$20,000 or less per year.

AOC provides the following comparisons on biweekly take-home pay for various salary categories that include impacts of typical deductions and the new federal tax rate schedule. It appears that take home pay will not substantially differ under the new federal tax rates and the temporary increase in the PERA employee contribution rate to 8.92 percent. The last column compares the bi-weekly paycheck as of February 2009 to the paycheck an employee will receive under the new effective federal tax rates and the contribution shift.

Public Employee Retirement Act

| Employee Category | Old Tax Table* 7.42% PERA | New Tax Table* 7.42% PERA | New Tax Table* 8.92% PERA | DIF |
|-------------------------|------------------------------|------------------------------|------------------------------|----------|
| \$30,536 not married | \$817.70 | \$835.10 | \$820.99 | \$3.29 |
| \$30,536 married | \$842.31 | \$872.11 | \$856.82 | \$14.51 |
| \$54,999 not married | \$1,383.08 | \$1,403.48 | \$1,381.24 | (\$1.84) |
| \$54,999 married | \$1,435.27 | \$1,466.02 | \$1,440.61 | \$5.33 |
| \$65,000 not married | \$1,588.38 | \$1,608.78 | \$1,582.50 | (\$5.89) |
| \$65,000 married | \$1,657.61 | \$1,688.36 | \$1,658.32 | 0.71 |

*Federal

Educational Retirement Act

| Employee Category | Old Tax Table* 7.9% ERA | New Tax Table* 7.9% ERA | New Tax Table* 9.4% ERA | DIF |
|-------------------------|----------------------------|----------------------------|----------------------------|----------|
| \$30,536 not married | \$755.55 | \$772.55 | \$757.94 | \$2.38 |
| \$30,536 married | \$662.49 | \$680.49 | \$662.88 | \$0.38 |
| \$54,999 not married | \$1,392.13 | \$1,412.13 | \$1,385.40 | (\$6.73) |
| \$54,999 married | \$1,349.07 | \$1,380.07 | \$1,351.34 | \$2.27 |
| \$65,000 not married | \$1,590.82 | \$1,597.77 | \$1,583.09 | (\$7.73) |
| \$65,000 married | \$1,619.91 | \$1,650.91 | \$1,619.41 | (\$0.50) |

*Federal

Synopsis of Original Bill

House Bill 854 increases the employee’s contributions made to the state’s public sector pension plans by 1.5 percent of an employee’s gross salary and decreases the employer’s portion of the contributions by a corresponding amount for the period from July 1, 2009 to June 30, 2011. After June 30, 2011, the employer and employee contribution rates would return to the amounts presently set by statute. The modification would apply to the ERB and the following pension plans managed by PERA:

- State General Member Plan 3
- State Police and Correctional Member Plan 1
- State Hazardous Duty Member Plan 2
- Judicial Retirement Act
- Magistrate Retirement Act.

FISCAL IMPLICATIONS

Employers

HB 854 would reduce employer operating budgets associated with the 1.5 percent reduction for pension contributions. The impact to the general fund is an estimated savings of \$42.6 million each year over a two year period, assuming salaries patterns remain constant over this period. The analysis assumes 100 percent of the employees pay employee contributions to pension plans; however, employee contributions are paid by the employer in the case of PERA return-to-work (RTW) employees and are not currently paid for ERB RTE employees. To offset this impact, Section 11 (A) House Bill 2 contains a provision that reduces the salaries by 1.5 percent for employees that have retired and returned to work under either the PERA or ERB return-to-work programs.

Employees

Employee salaries would be reduced by the 1.5 percent additional pension contribution. The tables below estimate the reductions to bi-weekly take-home pay.

| STATE AGENCY EMPLOYEES | |
|---|------|
| Salary=\$25,000 | \$14 |
| Average State Salary of \$42,100 | \$24 |
| Salary=\$75,000 | \$43 |
| PUBLIC SCHOOL EMPLOYEES | |
| Teachers (Average Salary = \$47,415) | \$27 |
| Instructional Staff (Average Salary = \$50,072) | \$29 |
| Other Certified and Non-Certified, inc. EA’s (Average Salary = \$23,734) | \$14 |
| Transportation (Average Salary = \$11,074) | \$6 |
| HIGHER EDUCATION EMPLOYEES | |
| Faculty – 4 Year (Average Salary = \$61,000) | \$35 |
| Faculty – 2 Year (Average Salary = \$46,156) | \$27 |

Employees do not pay taxes on the portion of their salaries for employee contributions. Increasing this contribution will reduce the marginal tax amount; thus, the impacts noted above would be slightly offset by paying fewer taxes. This amount would depend on the tax bracket and most likely would not be significant. It should also be noted that tax provisions in the American Recovery and Reinvestment Act will save workers approximately \$8 per week, according to the National Public Radio.

SPO points out exempt employees could see a 3.5 percent drop in salaries if the executive order to reduce those salaries is extended.

Actuarial Impact

The 1.5 percent swap will most likely not be cost-neutral to the pension funds. ERB explains the potential impact, as follows:

Shifting part of the employers' contribution to employees increases the amount that employees who terminate employment before retirement can withdraw from the fund. Ex-employees who take refunds receive their total contributions plus interest. The employers' contributions remain in the plan. Retaining employers' contributions decreases the total employer and employee contributions required to fund the pension plan and reduces the pension plans' unfunded accrued actuarial liability. Increasing the contributions that ex-employees can withdraw, while decreasing the employer contributions that remain in the fund, would have an adverse actuarial effect on the Educational Retirement Fund. Due to this effect, PERA's actuary estimates, every employee dollar is worth 95 cents of every employer dollar.

The actuarial effect over the two year time span in HB 854 has not been estimated. If the contribution shift were extended beyond two years, the actuarial effect could become more significant.

ERB also maintains the bill could have a second negative impact by possibly increasing the "death benefit" paid in the case of some ERB retirees who die before pension benefits equal the contributions they have paid into the pension plan. This impact is assumed not to be significant.

Operating Costs

PERA, ERB and employers would incur the cost of reprogramming their pension management software to change employer and employee contributions rates for 2010 and 2011. This cost is unknown, although SPO suggests that costs could offset some savings realized by employers. Pension staff employers would do some staff re-training, and website and other information would be changed; these costs should not be significant.

SIGNIFICANT ISSUES

The New Mexico Constitution requires a balanced budget. According to the February 2009 revenue estimate, FY10 recurring revenue will only support a base expenditure level that is \$575 million less than the FY09 appropriations before the 2009 solvency reductions. In addition, general fund reductions supplanted by federal stimulus funds will have to be restored: \$150 million in FY11 and \$330 million in FY12. HB 854 is part of a solvency package to meet the challenge of reduced revenues and balance the budget while maintaining essential services.

Average compensation for state employees has risen over 28 percent since 2003, from \$32.7 thousand per year to \$42.1 thousand per year in 2008. This increase in compensation far outstripped increases in the Consumer Price Index which increased by 16.8 percent for this same period in time. Average employer contributions for PERA increased over the same period from an average of \$5.4 thousand per employee per year in 2003 to \$6.9 thousand per year in 2008.

CONFLICT, RELATIONSHIP

HB 854 is a companion bill to House Bill 2, the General Appropriation Act, as follows:

Section 10. APPROPRIATION REDUCTIONS.--

A. General fund appropriations set forth in Section 4 of the General Appropriation Act of 2009 are reduced by the following amounts:

(2) a total of forty-two million five hundred ninety-nine thousand seven hundred dollars (\$42,599,700) to reflect temporary reductions in the employer contribution rates under the Public Employees Retirement Act and the Educational Retirement Act pursuant to House Bill 854 or similar legislation of the first session of the forty-ninth legislature provided that the reduction is contingent on the enactment of House Bill 854 or similar legislation of the first session of the forty-ninth legislature.

Section 11. APPROPRIATION REDUCTION FOR CERTAIN SALARY DECREASES.--

A. The general fund appropriation to each program, agency and public postsecondary educational institution in Section 4 of the General Appropriation Act of 2009 is reduced by an amount equal to one and one-half percent of the salary and benefits paid from the general fund to each employee of that program, agency or educational institution who:

(1) is a retired member under the Public Employees Retirement Act and has returned to work pursuant to Section 10-11-8 NMSA 1978 while continuing to receive a pension; or

(2) is a retired member under the Educational Retirement Act and has returned to work pursuant to Section 22-11-25.1 NMSA 1978 while continuing to receive a pension.

HB 854 relates or conflicts with the following bills:

- HJM 45 – PUBLIC EMPLOYEE & EDUCATION SOLVENCY PLANS STUDY
- HB 65 – LEGISLATIVE RETIREMENT CONTRIBUTIONS
- HB 79 – PUBLIC EMPLOYEE RETIREMENT INFO DISCLOSURE
- HB 236 – PERA SERVICE CREDIT PURCHASE (Expands service credit purchase)
- HB 246 – PERA RETURN TO WORK FOR CERTAIN EMPLOYEES
- HB 271/HB 355 – REOPEN MUNICIPAL EMPLOYEE RETIREMENT PLAN 4
- HB 351/SB 366 – RETIREE HEALTH CARE FUND CONTRIBUTIONS
- HB 525 – ALTERNATIVE EDUCATIONAL RETIREMENT PLANS
- HB 616 – PUBLIC RETIREES RETURNING TO WORK
- HB 631 – EDUCATIONAL RETIREMENT ELIGIBILITY
- HB 648 – JUDICIAL RETIREMENT FROM GENERAL FUND
- HB 683 – RETIRED PUBLIC EMPLOYEE RETURNING AS SHERIFF
- HB 684 – CONGRESSIONAL EMPLOYEE NM SERVICE CREDIT
- HB 721 – EDUCATIONAL RETIREES RETURNING TO WORK
- HB 731 – SESSION EMPLOYEE PERA CREDIT PURCHASES

- HB 765 – PUBLIC EMPLOYEES RETURNING TO WORK
- HB 798 – NEW PERA MEMBER ELIGIBILITY
- SB 145 – ELIMINATE END DATE FOR RETURN TO WORK
- SB 231 – PERA ELIGIBILITY FOR MUTUAL DOMESTICS
- SB 428 – RETIREE HEALTH DEFINITIONS & CONTRIBUTIONS
- SB 499 – MOTOR TRANSPORTATION OFFICER RETIREMENT

As currently worded, HB 573 proposes to require employees pick up the employee portion of pension contributions, which is currently being paid by the employer. If enacted as proposed, the 7.54 percent employee contribution would yield an approximate savings to employers of \$1.9 million based on a \$25.4 million payroll as of October 2008. However, this provision may be struck due to concerns regarding possible litigation. HB 616 would essentially end PERA’s RTW program after FY10 except where the governing body adopts a resolution to qualify the employee to work beyond a \$30,000 earnings cap.. To the extent RTW employees drop out of the program, new employees replacing them will pick up the employee portion of contributions.

Other bills that imply increases to employer costs would conflict with HB 854. Most notably, HB351 and the duplicate, SB 366, increase the employer and employee contribution rate for Retiree Health Care Authority from 1.95 percent to 3 percent over three years. SB 499 would increase the employer contribution rate by 8.51 percent for Motor Transportation officers. HB 648 would increase the employer rates for the Judicial Plan from 12 percent to 31.39 percent for judge salaries. HB 236 would increase the employer cost by expanding PERA members who can purchase up to five years service credit by requiring the employer to buy the first year. Finally, SB 476 requires ERB employers to pay the 7.9 percent employee portion of pension contributions currently not being paid.

TECHNICAL ISSUES

ERB points out that a negative actuarial impact on the fund due to enacting HB 854 might violate New Mexico Constitution: Article XX, Sec 22 states that the Legislature “shall not enact any law that increases the benefits paid by the system in any manner or changes the funding formula for a retirement plan unless adequate funding is provided.” The section also states that nothing in it “shall be construed to prohibit modifications to retirement plans that enhance or preserve the actuarial soundness” of an effected trust fund or plan. ERB concludes that if HB 854 bill did adversely affect a plan’s actuarial soundness, it could be found to be unconstitutional.

OTHER SUBSTANTIVE ISSUES

The tables below show the contribution rate changes for PERA and ERB.

HB854 Temporary Changes to Contribution Amounts

| Member Plan | Current Employee Contribution Rate | July 1, 2009 to June 30, 2011 Employee Contribution Rate | Current Employer Contribution Rate | July 1, 2009 to June 30, 2011 Employer Contribution Rate |
|-----------------------|---|---|---|---|
| General Member Plan 3 | 7.42% | 8.92% | 16.59% | 15.09% |
| State Police and | 7.60% | 9.10% | 25.10% | 23.60% |

| | | | | |
|------------------------------------|-------|-------|--------|--------|
| Adult Correctional Member Plan 1 | | | | |
| State Hazardous Duty Member Plan 2 | 4.78% | 6.28% | 25.72% | 24.22% |
| Judicial Retirement Act Plan | 7.50% | 9.00% | 12.00% | 10.50% |
| Magistrate Retirement Act Plan | 7.50% | 9.00% | 11.00% | 9.50% |

Source: NMSA 1978

| Member Plan* | Current Employee Contribution Rate | July 1, 2009 to June 30, 2011 Employee Contribution Rate | FY10 Employer Contribution Rate* | July 1, 2009 to June 30, 2011 Employer Contribution Rate |
|---------------------|---|---|---|---|
| ERB | 7.9% | 9.4% | 12.4% | 10.9% |
| ERB | 7.9% | 9.4% | 13.15% | 11.65% |

*Includes .75 employer contribution increase per year for FY10 and FY11.

WHAT WILL BE THE CONSEQUENCES OF NOT ENACTING THIS BILL

Pension contributions will remain as currently set in statute. The state budget will be about \$42.6 million short to meet revenue projections and balance the budget for FY10. Either taxes will need to be raised, reserves tapped, or other budget cuts would have to be implemented.

MA:GM/mc:svb