Report Highlights
Potential Costs and Impacts of HB 130 (Early Retirement Incentives) and HB 131 (COLA Increases)

House Resolution 299 calls on the LB&FC to study the potential costs and impacts of HB 130 and HB 131. Under HB 130, eligible members of the State Employee's Retirement System (SERS) and Public School Employee's Retirement System (PSERS) could retire without penalty after 30 years of service or if the member's age plus years of service totals 80 or more. These benefits would be available to SERS members who retire from July 1, 2006, through June 30, 2008, and to PSERS members who apply for retirement during March 1 through June 1 (with an effective date no later than July 1) in either 2006 or 2007. HR 131 would provide automatic cost-of-living adjustments to annuitants based on the CPI. The LB&FC contracted with Milliman to conduct a comprehensive study of these proposals.

Findings:

Current and Projected Status of SERS and PSERS. Although the most recently reported funded ratios (assets to liabilities) are relatively sound for both SERS (95%) and PSERS (85%), these ratios are projected to deteriorate through the end of FY 2011-12 to 82% for SERS and 77% for PSERS. This would place both systems below the median of the other large public sector retirement systems surveyed. Future movement toward private sector accounting rules could further adversely affect the reported funded status.

Current and Projected Employer Contributions. In FY 2005-06, employer contributions for SERS members are 3.02% of payroll and for PSERS, 4.0%. In FY 2012-13, SERS and PSERS employer contribution rates are scheduled to jump to 20.16% and 21.23% of payroll respectively, due primarily to pension provisions enacted in 2001 and 2002 and adverse investment returns in the early 2000s.

Impact of HB 130. Payroll savings due to the early retirement incentives proposed in HB 130 are estimated at $631 million for SERS members and $2.0 billion for PSERS members for the 10-year period ending June 30, 2016. However, during this 10-year period employer pension contributions would increase by an estimated $402 million (SERS) and $1.435 billion (PSERS). Additional health care costs for the new retirees would total about $515 million for SERS members and about $68 million for PSERS members. (PSERS members receive a much-reduced health insurance benefit after retirement.) Thus, the total net cost of offering the early retirement incentives in HB 130 to SERS members is estimated to be $286 million. The comparable figure for PSERS members is a net savings of $503 million.

Impact of HB 131. For various reasons cited in the report, Milliman did not believe the COLA provisions, as structured in HB 131, to be feasible. Instead, and as provided for in HR 299, Milliman estimated the cost of a COLA that would: (1) be limited to 3% per annum, (2) only be provided after an annuitant attained superannuation age and after they had been retired 12 months or more, and (3) not be provided to survivor annuitants. Under such a plan, annual employer contributions to SERS would increase by an estimated $1.2 billion a year for each of the next 10 years; for PSERS, the increase would be $2.7 billion per year. An unlimited COLA, as provided for by HB 131, could cost significantly more.

Other COLA Variations. The report also provides cost estimates of other possible COLA approaches, including *partial indexing* (FY 2007-08 costs to provide 50% of CPI: $486 million for SERS and $1.175 billion for PSERS); a *deferred COLA*, where COLA begin 10 years after the later of actual retirement or superannuitant eligibility (FY 2007-08 costs estimated at $425 million for SERS and $1.045 billion for PSERS); and an *ad hoc COLA* (FY 2007-08 costs for a one-time, 4% ad hoc COLA for annuitants that retired prior to July 1, 2001, are estimated at $39 million for SERS and $89 million for PSERS).

Recommendations:

1.) The Commonwealth should develop a long-term plan to finance already-enacted SERS and PSERS benefits before adding new benefits.

2.) If an early retirement incentive is offered, allow school districts to "opt-out" of the incentive to avoid the loss of too many employees with critical skills or experience.

For a copy of the report, please call 717-783-1600 or e-mail us at info@lbfc.legis.state.pa.us

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