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**REVISED
FISCAL NOTE**

(replaces fiscal note dated March 13, 2018)

Drafting Number: LLS 18-0477 **Date:** March 15, 2018
Prime Sponsors: Sen. Tate; Priola **Bill Status:** Senate Finance
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Bill Topic: MODIFICATIONS TO PERA TO ELIMINATE UNFUNDED LIABILITY

Summary of Fiscal Impact:

<input checked="" type="checkbox"/> State Revenue	<input type="checkbox"/> TABOR Refund
<input checked="" type="checkbox"/> State Expenditure	<input checked="" type="checkbox"/> Local Government and School District
<input type="checkbox"/> State Transfer	<input checked="" type="checkbox"/> Statutory Public Entity

This bill makes modifications to the Colorado Public Employees' Retirement Association (PERA). It creates ongoing state revenue reductions, state and local expenditure increases, and increases net revenue to PERA.

Appropriation Summary: The bill requires an appropriation of at least \$17.5 million in FY 2018-19, split between every state agency.

Fiscal Note Status: The fiscal note reflects the introduced bill and represents a preliminary analysis. It has been revised to include additional information about the impact to local governments and schools.

**Table 1
State Fiscal Impacts Under SB 18-200**

		FY 2018-19	FY 2019-20
Revenue	General Fund Total		<i>Reduction. Not estimated.</i>
Expenditures	General Fund	at least \$9.6 million	at least \$19.2 million
	Cash Funds	at least \$4.3 million	at least \$8.5 million
	Reappropriated Funds	at least \$1.9 million	at least \$3.9 million
	Federal Funds	at least \$1.7 million	at least \$3.5 million
	Total	at least \$17.5 million	at least \$35.1 million
Transfers		-	-

Summary of Legislation

This bill makes several changes related to the Colorado Public Employees' Retirement Association (PERA). These are described in order of the bill.

Change to number of years in the highest average salary calculation. Under current law, the retirement benefit paid to a PERA member depends on his or her date of hire, years of service credit, and age at retirement, and is calculated using a percentage of the member's highest annual salary (HAS) over a period of time, including a base salary year. The bill changes the number of years factored into the HAS calculation for members who are not vested by or are hired on or after January 1, 2020, as shown in Table 2.

Table 2
Highest Annual Salary Period Under SB 18-200 After Base Year
on or after January 1, 2020

As of 1/1/20	All Divisions except Judicial	Judicial
Vested	3 periods of 12 months	1 period of 12 months
Not Vested or New Member	7 periods of 12 months	3 periods of 12 months

Salary definition. The bill modifies the definition of salary so that pre-tax payroll deductions are counted towards salary, as is unused sick leave converted to cash payments. The bill clarifies that insurance premiums paid by employers are not counted as salary.

Requirements for local government employers that terminate PERA affiliation. The bill clarifies provisions related to a local government division employer that ceases operations or participation in PERA, so that when an employer has terminated its affiliation with PERA, it is the PERA board that determines the amount to be paid by that employer to fully fund its share of the unfunded liability of the defined benefit plan and of the health care trust fund. The board's determination may be appealed by the employer through the administrative review process established in PERA rule. The local government's employees become inactive members of PERA effective on the termination date, and may elect to have their member contributions credited to an alternative pension plan or refunded. In the absence of such election, the member contributions will remain with PERA.

Increase in employer and member contribution rates. The bill increases the PERA employer contribution rates by the percentages and schedules shown in Table 3. These increases are credited to PERA's defined benefit trusts regardless of employee's plan election.

Table 3
Phase-in of 2% Employer Contribution Rate Increase Under SB 18-200

	State	Troopers	School	DPS	Local	Judicial
Current Law*	10.15%	12.85%	10.15%	10.15%	10.0%	13.66%
As of 7/1/18	11.15%	13.85%	11.15%	11.15%	11.0%	14.66%
As of 1/1/19	12.15%	14.85%	12.15%	12.15%	12.0%	15.66%

The bill also increases the PERA employee contribution rates by the percentages shown in Table 4. These rates are multiplied by gross salary under the bill.

**Table 4
 Phase-in of 3% Member Contribution Rate Increase Under SB 18-200**

	State	Troopers	School	DPS	Local	Judicial
Current Law	8.0%	10.0%	8.0%	8.0%	8.0%	8.0%
As of 7/1/18	8.5%	10.5%	8.5%	8.5%	8.5%	8.5%
As of 1/1/19	9.0%	11.0%	9.0%	9.0%	9.0%	9.0%
As of 7/1/19	10.0%	12.0%	10.0%	10.0%	10.0%	10.0%
As of 1/1/20	11.0%	13.0%	11.0%	11.0%	11.0%	11.0%

Automatic contribution and cost of living rate adjustments. Beginning January 1, 2020, the bill requires employer and employee contribution rates and the cost of living adjustment (COLA) to remain unchanged unless triggered by certain circumstances, as shown in Table 5. These increased amounts rely on the following definitions in the bill:

- *"Weighted average"* means the most recent valuation of the proportion of unfunded actuarial accrued liability attributable to each division.
- *"Blended total contribution amount"* is the weighted average of the total amounts paid by employers and members to PERA by all divisions, not to include the portions of employer contributions remitted to the health care trust fund and the COLA reserve.
- *"Blended total required contribution"* is the weighted average of the total reported actuarially determined contribution rates and member contribution rates for PERA's trusts.

When the blended total contribution amount is less than 98 percent or more than 110 percent of the blended total actuarially required contribution, adjustments must be determined by PERA, equally apportioned, and be the maximum yearly adjustment allowed with certain exceptions. Adjustments may occur only once in a calendar year.

**Table 5
 Automatic Contribution and COLA Rate Adjustments Under SB 18-200**

When the blended total contribution amount is less than 98% of the blended total actuarially required contribution:

COLA Rate	reduced up to 0.25%; not to be reduced to less than 0.5% total
Employer Contribution Rate	increased up to 0.5%; not to exceed statutory contribution rates plus 2% total
Member Contribution Rate	increased up to 0.5%; not to exceed statutory contribution rates plus 2% total

When the blended total contribution amount is greater than or equal to 110% of the blended total actuarially required contribution:

COLA Rate	increased up to 0.25%; not to exceed 2% total
Employer Contribution Rate	reduced up to 0.5%; not to be less than statutory contribution rates
Member Contribution Rate	reduced up to 0.5%; not to be less than statutory contribution rates

Defined contribution supplement. Beginning January 1, 2022, the bill requires an adjustment to each PERA division's employer contribution rates in order to include a defined contribution supplement. The defined contribution supplement will be the amount that would have otherwise gone to the defined benefit trusts to pay down the unfunded liability, plus investment earnings on that amount, and will be made on behalf of employees who begin employment on or after January 1, 2020.

Earned service credit for part-time work for new members. The bill modifies the way service credit is earned for part-time work for PERA members who begin employment on or after January 1, 2020. These members earn a full year of service credit for 12 months of employment if the member works full time or works at least 8 months but less than 12 months in a year. However, if the member does not work full time, the earned service credit will be determined by the ratio of part-time work to full-time work and the number of months for which contributions are remitted to the number of months required for a year of service credit.

Service retirement and reduced service retirement eligibility for new and current members. For PERA members who begin employment on or after January 1, 2020, the bill modifies service retirement eligibility as shown in Table 6, and specifies that no contractual right is created related to these age requirements. The bill also modifies the reduced service retirement eligibility as shown in Table 7. In addition, individuals, with the exception of state troopers, who are current PERA members as of December 31, 2019, must be the age specified on the table, plus one year for every four years that the member's age is less than 46 years on January 1, 2020, not to exceed 65 years for any member in order to be eligible for regular or reduced retirement.

Table 6
Service Retirement Eligibility Under SB 18-200
for members hired on or after January 1, 2020

Division	Years of Service Required to Retire at Any Age		Years of Service Required to Retire at a Specific Retirement Age		Years of Service Required to Retire at Age 65	
	<i>Current Hires</i>	<i>SB 18-200</i>	<i>Current Hires</i>	<i>SB 18-200</i>	<i>Current Hires</i>	<i>SB 18-200</i>
State, Local, and Judicial	35 years	40 years	Age 60, 30 years	No specific age	5 years	5 years
Troopers	30 years	35 years	Age 50, 25 years Age 55, 20 years	Age 55, 25 years	5 years	5 years
School and DPS	35 years	40 years	Age 58, 30 years	No specific age	5 years	5 years

Table 7
Reduced Service Retirement Eligibility Under SB 18-200
for members hired on or after January 1, 2020

	Current Law		SB 18-200	
	Age Requirement	Service Credit Requirement	Age Requirement	Service Credit Requirement
All Divisions	50 years old 55 years old 60 years old	25 years of service 20 years of service 5 years of service	55 years old 60 years old	25 years of service 5 years of service
State Troopers	50 years old	20 years of service	50 years old	20 years of service

Cost of living adjustment. The annual cost of living adjustment (COLA) for benefit recipients who began membership prior to January 1, 2007, is currently 2 percent. For the years 2018 and 2019, the bill reduces the COLA to 0 percent. For each year thereafter, the bill sets the COLA at 1.25 percent. This amount may be otherwise adjusted by the automatic adjustment provisions explained above. The bill also requires benefit recipients whose effective date of retirement is on or after January 1, 2011, and who have not received a COLA on or before May 1, 2018, to receive retirement benefits for at least three years following retirement before receiving a COLA adjustment.

Defined contribution plan. Currently, members in the state division hired after January 1, 2006, may elect to participate in PERA's defined contribution plan rather than its defined benefit plan. Under current law, a defined contribution account receives the monthly employer contribution, as outlined in Table 3 above, while the amortization equalization disbursement (AED) and supplemental amortization equalization disbursement (SAED) payments are credited to pay down the unfunded liability of the defined benefit plan. Beginning January 1, 2020, anyone hired in the school, Denver Public Schools, local government, and judicial divisions may elect to participate in the defined contribution plan. An employee who elects the defined contribution plan will receive their full employee contribution amount, and the employer contribution amount under current law. The additional employer contribution amount created by the bill will be credited to pay down the unfunded liability of the defined benefit plan.

Public Pension Legislative Oversight Committee. The bill replaces the existing Police Officers' and Firefighters' Pension Reform Commission with the Public Pension Legislative Oversight Committee, which is required to study and develop proposed legislation relating to the funding and benefit designs of PERA and the Fire and Police Pension Association. The committee is comprised of four senators appointed by the Senate President; six representatives appointed by the House Speaker; and four experts in the area of pensions or retirement plan designs appointed by the State Treasurer. The committee may commission an independent review of the economic and investment assumptions used to model the PERA financial situation every three years.

State Revenue and TABOR Impact

The bill's change in salary definition and increase in employee contributions will reduce taxable income for PERA members. In addition, the bill's highest annual salary calculation and COLA reduction will reduce benefit payments from the PERA trusts, which will also reduce state tax collections. This General Fund reduction has not been estimated.

State revenue is not currently expected to exceed the TABOR limit in the current forecast period and no refund will be required; however, refunds in future years when the state next collects a TABOR refund obligation will be reduced.

State Expenditures

This bill will increase state expenditures by at least \$17.5 million in FY 2018-19, and by at least \$35.1 million in FY 2019-20 and each year thereafter, as shown in Table 8.

Assumptions. This fiscal note uses the Joint Budget Committee's (JBC's) estimated salary base for FY 2018-19 to evaluate employer and employee contribution increases. The JBC estimates include adjustments approved for the current fiscal year related to salary and staffing increases, but do not include supplemental or pending legislation, which may add to the base. The fiscal note does not include proposed merit pay increases or a rate of inflation, nor does it delineate between employee retirement plan elections.

In addition, as of this writing, the fiscal note does not estimate:

- future automatic adjustments, up to 2 percent, of the employer and employee contribution rates;
- the future cost of the defined contribution supplement;
- the impact on the value of the PERA benefit as it relates to the state's total compensation plan, nor any change to employee behavior related to retention and retirement; nor
- the impact to institutions of higher education.

Employer contributions. As discussed in the Assumptions section, employer contributions have been calculated using the Joint Budget Committee's estimated salary base for FY 2018-19 and reflect the 1 percent and 2 percent increases under the bill. The estimated salary base is assumed to reflect gross salary and includes no growth assumptions. Precise impacts to each state agency's personal services lines have not been estimated, and will be provided in a future fiscal note.

**Table 8
 State Employer Contribution Increase Under SB 18-200***

FY	% Increase	General Fund	Cash Funds	Reappropriated Funds	Federal Funds	Total Funds
18-19	1%	\$9,622,253	\$4,254,615	\$1,933,840	\$1,735,968	\$17,546,676
19-20	2%	\$19,244,505	\$8,509,229	\$3,867,680	\$3,471,936	\$35,093,350

* Uses JBC's FY 2018-19 estimated salary base. Totals may not sum due to rounding.

Employee contributions. Total employee contributions are expected to increase by at least \$13.2 million in FY 2018-19, and by at least \$43.9 million in FY 2019-20, using the estimated salary base.

Automatic rate adjustments. Beginning in the second half of FY 2019-20, the bill creates a mechanism in statute to automatically raise or lower the employer and member contribution rates, as shown in Table 5. If these adjustment mechanisms are triggered, employer and member

contributions may increase up to 0.5 percent per year, capped at an additional overall 2 percent. As such, the amounts shown in Table 8 and discussed under employer contributions could increase up to 2 percent in future years. The fiscal note assumes that these rate adjustments will be addressed during the annual budget process.

Defined contribution supplement. Beginning in the second half of FY 2021-22, the bill requires an adjustment to the employer contribution rate equal to the amount that would have otherwise gone to the defined benefit trusts to pay down the unfunded liability, plus any investment earnings on that amount, that occur as a result of defined contribution plan elections by employees hired after January 1, 2020. This additional contribution is conditional on the financial health of the PERA trusts and has not been estimated.

Total compensation. If the value of the state's retirement benefit is reduced in a future annual compensation report, state expenditures will increase. This potential impact has not been estimated.

All state agencies. All state agencies will have an increase in workload and costs to update employee information and process the new payroll deductions.

Public Pension Legislative Oversight Committee. Legislative Department expenditures will increase for per diem and staffing costs related to the Public Pension Legislative Oversight Committee. Because it replaces an existing committee of the same size and scope, however, these costs do not require an appropriation. The committee may commission an independent review of the assumptions used to model the PERA financial situation, which is expected to cost \$200,000 per contracted study. This amount will be requested as needed through the annual budget process.

Local Governments and Special Districts

Beginning in the current FY 2017-18, the bill will increase expenditures for local governments. For informational purposes, PERA's estimate of the cumulative impact to the local government division is provided in Table 9. PERA's estimate uses December 31, 2016, divisional payroll and include a payroll growth projection of 3.5 percent. In addition, a few examples of specific local government impacts are provided following Table 9.

Background. According to the most recent PERA comprehensive annual financial report, the local government division is comprised of 1 county, 27 municipalities, and 120 special districts.

Budgetary concerns for local governments. Local governments are on a calendar year budget that is typically finalized in October of the prior year. The bill will result in budgetary requirements for CY 2018 that have not been accounted for and may require funding from other programs to keep local government budgets balanced.

Additionally, the bill's requirement to use the gross salary amount (which includes health- and transportation-related pre-tax deductions) to calculate the PERA benefit is effective upon signature of the Governor, and requires immediate budgeting in advance of July 1, 2018.

Table 9
PERA Estimates of Local Government Division Impacts Under SB 18-200

Year	Contributor	Impact Type	Amount
FY 18-19	Local Gov't Employer	Contribution Rate Increase	\$6,500,000
		Change in Gross Salary Definition Increase	\$2,700,000
		Subtotal	\$9,200,000
	Local Gov't Employee	Contribution Rate Increase	\$4,900,000
		Change in Gross Salary Definition Increase	\$1,100,000
		Subtotal	\$6,000,000
	TOTAL	\$15,200,000	
FY 19-20	Local Gov't Employer	Contribution Rate Increase	\$13,400,000
		Change in Gross Salary Definition Increase	\$2,900,000
		Subtotal	\$16,300,000
	Local Gov't Employee	Contribution Rate Increase	\$16,700,000
		Change in Gross Salary Definition Increase	\$1,400,000
		Subtotal	\$18,100,000
	TOTAL	\$34,400,000	
FY 20-21	Local Gov't Employer	Contribution Rate Increase	\$13,800,000
		Change in Gross Salary Definition Increase	\$3,000,000
		Subtotal	\$16,800,000
	Local Gov't Employee	Contribution Rate Increase	\$20,800,000
		Change in Gross Salary Definition Increase	\$1,500,000
		Subtotal	\$22,300,000
	TOTAL	\$39,100,000	

Source: Colorado Public Employees' Retirement Association. Totals have been rounded.

Local government examples. The impact of the employer contribution increase on local governments will vary by the size of the local government and its number of employees. The fiscal note highlights three examples that are representative of a large, medium-sized, and small local government. The amounts shown reflect calendar years.

Boulder County — large. Boulder County expenditures are expected to increase by approximately \$670,000 in CY 2018, \$2.0 million in CY 2019, and \$2.7 million in CY 2020 and thereafter. Its employees will contribute an additional \$700,000 in CY 2018, \$2.8 million in CY 2019, and \$4.2 million in FY 2020.

Colorado Springs — medium. City of Colorado Springs expenditures are expected to increase by approximately \$600,000 in CY 2018, \$1.7 million in CY 2019, and \$2.5 million in FY 2020-21. Its employees will contribute an additional \$400,000 in CY 2018, \$1.5 million in CY 2019, and \$2.6 million in CY 2020.

Alamosa — small. City of Alamosa expenditures are expected to increase by approximately \$16,000 in CY 2018 and \$32,000 in CY 2019. Its employees will contribute an additional \$8,300 in CY 2018 and \$24,000 in CY 2019. Alamosa's CY 2020 figures were not available as of this writing.

School Districts

Beginning in the current FY 2017-18, the bill will increase expenditures for school districts. For informational purposes, PERA's estimate of the cumulative impact to the school division (not including Denver Public Schools, which is a separate PERA division) is provided in Table 10. PERA's estimates use December 31, 2016, divisional payroll and include a payroll growth projection of 3.5 percent.

Table 10
PERA's Estimates of School Division Expenditures Under SB 18-200

Year	Contributor	Impact Type	Amount
FY 18-19	District	Contribution Rate Increase	\$46,200,000
		Change in Gross Salary Definition Increase	\$19,500,000
		Subtotal	\$65,700,000
	District Employee	Contribution Rate Increase	\$34,700,000
		Change in Gross Salary Definition Increase	\$8,100,000
		Subtotal	\$42,800,000
	TOTAL	\$108,500,000	
FY 19-20	District	Contribution Rate Increase	\$95,600,000
		Change in Gross Salary Definition Increase	\$21,200,000
		Subtotal	\$116,800,000
	District Employee	Contribution Rate Increase	\$119,700,000
		Change in Gross Salary Definition Increase	\$10,000,000
		Subtotal	\$129,700,000
	TOTAL	\$246,500,000	
FY 20-21	District	Contribution Rate Increase	\$99,000,000
		Change in Gross Salary Definition Increase	\$21,900,000
		Subtotal	\$120,900,000
	District Employee	Contribution Rate Increase	\$148,500,000
		Change in Gross Salary Definition Increase	\$10,900,000
		Subtotal	\$159,400,000
	TOTAL	\$280,300,000	

Source: Colorado Public Employees' Retirement Association. Totals have been rounded.

Denver Public Schools. Denver Public Schools merged its retirement system with PERA in 2009, and has its own PERA trust as a result. The impact to Denver Public Schools (DPS) is shown in Table 11. Contribution rate increase impacts use DPS's covered payroll projections for each calendar year calculated to match fiscal years, and assume growth of 3.04 percent in CY 2018 and 3.5 percent each year thereafter. Net to gross salary increases are based on actual FY 2017-18 totals through February 2018, with projections for remainder of the fiscal year, and a 7 percent expense increase for each year thereafter.

Table 11
Denver Public Schools Division Expenditures Under SB 18-200

Year	Contributor	Impact Type	Amount
FY 18-19	DPS	Contribution Rate Increase	\$7,092,681
		Change in Gross Salary Definition Increase	\$9,528,305
		Subtotal	\$16,620,986
	DPS Employees	Contribution Rate Increase	\$5,350,008
		Change in Gross Salary Definition Increase	\$3,941,970
		Subtotal	\$9,291,978
TOTAL			\$25,912,964
FY 19-20	DPS	Contribution Rate Increase	\$14,681,850
		Change in Gross Salary Definition Increase	\$10,677,333
		Subtotal	\$25,359,183
	DPS Employees	Contribution Rate Increase	\$18,415,441
		Change in Gross Salary Definition Increase	\$5,061,490
		Subtotal	\$23,476,931
TOTAL			\$48,836,114
FY 20-21	DPS	Contribution Rate Increase	\$15,195,715
		Change in Gross Salary Definition Increase	\$11,424,746
		Subtotal	\$26,620,461
	DPS Employees	Contribution Rate Increase	\$22,793,573
		Change in Gross Salary Definition Increase	\$5,673,689
		Subtotal	\$28,467,262
TOTAL			\$55,087,723

Source: Denver Public Schools.

PERACare. Defined contribution plan participants are not eligible for the disability, survivorship, and retiree health care benefits that defined benefit plan participants are eligible for; however, defined contribution plan members may enroll in PERACare, PERA's health insurance plan. If local employers elect to offer this benefit to defined contribution plan participants, their costs will increase. These impacts have not been estimated.

Statutory Public Entity Impact

The bill will increase revenue to the PERA trusts, with the exception of its health care trusts.

Projected actuarial funded status for PERA's trusts. The bill reduces the estimated amortization periods necessary to eliminate the unfunded actuarial accrued liability in all of PERA's trusts, as shown in Table 12.

Table 12
PERA's Unfunded Liability Under SB 18-200

Division	Amortization Period Under Current Law	Amortization Period Under SB 18-200
State	57 years	24 years
School	77 years	24 years
Local Government	54 years	14 years
Judicial	53 years	19 years
Denver Public Schools	55 years	20 years

Source: Colorado Public Employees' Retirement Association. Based on 2016 valuation.

Cost of living adjustment impact. The bill's adjustment to the COLA payment is expected to reduce PERA benefit payments by \$92.2 million in FY 2018-19 and \$65.5 million in FY 2019-20. This estimate uses an annualized January 2018 benefit payroll and applies 0 percent increase in 2018 and 2019, and 1.25 percent increase for 2020. The impact to future PERA benefit payments as a result of the three-year timeout for benefit recipients whose effective date of retirement is on or after January 1, 2011, and who have not received a COLA on or before May 1, 2018, has not been estimated.

Automatic rate adjustments. The fiscal note has not estimated the potential revenue increase to PERA's trusts from the automatic COLA, employer, and employee rate contributions as of this writing.

Defined contribution supplement. Beginning in 2022, PERA will annually calculate an additional employer contribution rate to be paid by each division to supplement the amount that would have otherwise gone to the defined benefit trusts to pay down the unfunded liability, plus any investment earnings on that amount, that occur as a result of defined contribution plan elections for employees hired after January 1, 2020. The potential additional contribution is conditional on the financial health of the PERA trusts. Because of this mechanism, any impact to PERA's trusts resulting from members electing the defined contribution plan will be offset by the defined contribution supplement paid by each division.

Impact on the PERA health care trust funds. The defined contribution election will have a negative impact on the PERA health care trust funds. PERA assumes, based on state division participation, that 12 percent of division employees will elect the defined contribution plan, which will result in an extended amortization period for these divisional health care trust funds. The fiscal note has not estimated this decrease.

Effective Date

The bill takes effect upon signature of the Governor, or upon becoming law without his signature.

State Appropriations

The bill requires an appropriation of at least \$17.5 million in FY 2018-19, split between every state agency. The appropriation amount for each agency has not yet been estimated and will be provided in a future fiscal note.

State and Local Government Contacts

All State, Local, and Statutory Agencies