"FISCAL NOTE. -- "This bill would amend various sections of the Education Law, the Retirement and Social Security Law, and the Administrative Code of the City of New York to implement a new retirement benefit structure (Tier 6) for members who first join a public retirement system of the state or New York City on or after April 1, 2012. Tier 6 would provide two different plan options – a defined benefit plan (DB Plan) similar to the benefit plan for members of earlier Tiers, and a defined contribution plan (DC Plan) in which separate accounts are established for each member similar to a 401(k) plan. A Tier 6 member desiring to elect the DC Plan must do so within the first 30 days of service. The member's election is irrevocable. The remainder of this fiscal note provides descriptions and costs with respect to the New York State Teachers' Retirement System.

Plan Benefits:

DB Plan: Members would be eligible for a retirement benefit payable monthly for life upon retirement. Eligibility for a service retirement benefit would require the rendering of a minimum of twelve years of credited service and attainment of age 65. Members would not be permitted to receive a service or vested retirement benefit prior to the attainment of age 65. The service retirement benefit formula for years of service up to 30 would be equal to one-sixtieth of final average salary times years of service. Years of service above 30 would have a benefit multiplier of 1.5%. Final average salary would be determined as the average of the highest five consecutive years of salary. Salary in a given year in excess of eight percent over the average of the four previous years would not be included in the final average salary. A death benefit of up to three times salary is provided upon the death of a member in service. A disability benefit is provided to members who become disabled while in service. Members who withdraw before becoming vested receive a refund of their employee contributions, and accumulated interest of 5% per year.

DC Plan: Members would have individual accounts, similar to a 401(k) plan, and at retirement would receive whatever amount is in their account. Accounts would consist of the sum of contributions made and any investment income earned. No specific benefit amount at retirement is promised. Members would receive a basic annual contribution of 4% of pay from employers. Employers would also contribute up to an additional 3% of pay as a matching contribution to an employee's own contribution, if the employee contributed. A death benefit of up to three times salary is provided upon the death of a member in service. No disability benefit is provided. No employer contribution is required to be made until the participant has been a member of the Retirement System for one full plan year. All employer contributions are immediately and fully vested when made.

Plan Costs - Employee:

DB Plan: Members in the DB Plan shall be required to contribute either 4%, 5%, or 6% of salary annually depending on their salary level as follows – members whose wages are equal to $35,000 or less shall contribute 4%, members with wages between $35,001 and $69,000 shall contribute 5%, and members with wages above $69,000 shall contribute 6%.

If the required employer contribution rate (ECR) associated with Tier 6 members exceeds 7%, employees will be required to contribute an additional amount equal to one-half of the difference between the ECR and 7%. Conversely If the ECR associated with Tier 6 members is less than 4%, the employee contribution rate will be reduced by an amount equal to one-half of the difference between 4% and the ECR.

DC Plan: Members in the DC Plan are not required to make any employee contribution. Members may opt to make employee contributions to their accounts up to the maximum amount permitted by federal law.

Plan Costs - Employer:

DB Plan: The employer contribution rate (ECR) is determined annually by actuarial valuation, and represents the amount required to maintain appropriate actuarial funding. The long-term expected actuarially-determined ECR for the proposed Tier 6 benefit structure is 3.8% of pay. This rate includes the cost of the death benefit, and the cost of the plan's administrative expenses. The actual ECR in a given year will be higher or lower than this amount, depending on plan experience, in particular the plan's investment experience. In accordance with current actuarial assumptions however the expected employer contribution rate is **3.8%** of pay.

If the plan's ECR associated with Tier 6 exceeds 7%, then the employees must share in the cost of this excess, and similarly if the ECR is below 4%, the employees benefit from this reduction, as described in the *"Plan Costs – Employee"* section above. For example, if the Tier 6 ECR in a given year is 9%, then employers will pay 8%, and employees an additional 1%. Conversely if the Tier 6 ECR is 2%, then employers will pay 3%, and employees will have a 1% reduction in their required employee contribution rate.

DC Plan: Employers are required to contribute a basic annual contribution rate of 4% of pay. In addition, employers are required to provide a matching contribution on employee contributions of up to an additional 3% of pay. Therefore employers will need to budget a 7% of pay annual expense as they will not know in advance which employees will elect to contribute and how much. Additionally employers will need to contribute an annual amount, as determined by the Retirement System, to cover the cost of the death benefit provided under the plan, as well as an amount to cover the cost of administering the plan. Although the specifics regarding these last two items are as yet unknown, it is roughly estimated that an additional 1% employer contribution should be anticipated. All together this brings the expected ECR for the DC Plan to **8%** of pay.

Additionally it is expected that there would be a significant start-up cost for a state-wide DC plan of this type. Although no specific estimate of this start-up cost has as yet been determined, it is expected that it would be in the millions of dollars.

Administrative Concerns/Costs:

The Retirement System does not currently have a DC Plan platform which can be adapted to this proposal. Tier 6 would therefore represent a significant expansion of administrative responsibilities and workload for the Retirement System. Although the bill permits NYSTRS to hire outside vendors as needed, these vendors would need to be carefully identified and selected. It is highly unlikely that a DC Plan could be established and functioning by the bill's effective date of April 1, 2012.

The DB Plan can in almost all respects be administered programmatically, although additional computer programming and additional administrative procedures will be required. The graded employee contribution rate schedule (4%/5%/6%) in the Tier 6 DB Plan would represent considerable ongoing administrative difficulties however. Required employee contributions are withheld by employers from employee paychecks throughout the year, which requires that employers know the correct employee contribution rate percentage in advance. Under this bill the correct percentage may not be known until after the last paycheck of the year. Wages paid during the plan year would have to be reviewed after the end of the plan year on a member by member basis, and overpayments or underpayments of member contributions addressed accordingly.

Background/Additional Information:

"The current required employer contribution rate for the New York State Teachers' Retirement System is 11.11% of pay, applicable to 7/1/11 – 6/30/12 member salaries and to be collected in the fall of 2012. This rate is estimated to increase to 11.84% for the 7/1/12- 6/30/13 fiscal year. This rate is applicable to the salaries of all members, regardless of tier. Even if no additional members joined the defined benefit plan after April 1, 2012, the annual cost of this plan for the current 430,000 members and retirees that participate in it would go on for several decades.

"Our "new entrant rate", a hypothetical employer contribution rate that would occur if we started a new Retirement System without any assets, is equal to 10.9% of pay under the Tier 4 benefit structure and 7.9% of pay under the Tier 5 benefit structure, in accordance with the Retirement System's current actuarial assumptions. This can be thought of as the long-term expected cost of the benefit structure, based on current actuarial assumptions. For the proposed Tier 6 DB Plan benefit option, this new entrant rate would be equal to 3.8% of pay.

"The source of this estimate is Revised Fiscal Note 2012-8 dated February 2, 2012 prepared by the Actuary of the New York State Teachers' Retirement System and is intended for use only during the 2012 Legislative Session. I, Richard A. Young, am the Actuary for the New York State Teachers' Retirement System. I am a member of the American Academy of Actuaries and I meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein."

"FISCAL NOTE. "This bill would require new members who first join public retirement systems in New York State on or after April 1, 2012 to become covered under the provisions of a new defined benefit plan or a new defined contribution plan.
"The proposal does not appear to provide sufficient time for the provisions to be implemented by April 1, 2012.
"Insofar as this bill would affect the New York State and Local Employees Retirement System (ERS), the significant design changes to the defined benefit plan include:
1. Employee contributions of X+Y% of pay for all years of service, except members enrolled in a plan that limits the amount of creditable service that may be accrued would

not be required to contribute after accruing the maximum amount of creditable service under such plan,

where X is determined as follows:

if the annual pay rate is $32,000 or less then X = 4.0%
if the annual pay rate is $32,001 to $63,000 then X = 5.0%
if the annual pay rate is $63,001 or more then X = 6.0%

and Y is determined as follows:

if the individual's plan has a <u>total</u> contribution rate (T) for the fiscal year that is greater than 7%, then Y = (T – 7%) /2
if the individual's plan has a <u>total</u> contribution rate (T) for the fiscal year that is less than 4%, then Y = (T – 4%) /2
otherwise Y = 0%

2. The service retirement benefit would be one-sixtieth (1.67%) of FAS for the first 30 years of creditable service, and three-two hundredths (1.50%) of FAS in excess of 30 years,

3. Members in regular plans (where retirement eligibility requires the attainment of a certain age as well as the accumulation of a certain amount of service credit) must attain age 65 before they may receive a service retirement benefit,

4. Final average salary (FAS) would be based on a 5 year average, with no year's salary permitted to exceed 8% of the average of the previous 4 year's salary,
5. Annual overtime paid at a rate greater than the standard rate of pay would not be included in the definition of wages and final average salary,
6. Reportable salary (for a fiscal year) may not exceed the salary of the Governor of the state New York, which currently is set in law to be $179,000 (the reportable salary would change when the Governor's salary does),
7. Lump sum vacation pay, any form of termination pay and additional compensation paid in anticipation of retirement would no longer be included in a member's final average salary,
8. Service credit for unused sick leave time would no longer be granted,
9. Twelve year vesting.

"If this bill is enacted, NYSLRS would calculate new plan rates for all ERS members who first enter on or after April 1, 2012. The long term expected annual employer <u>normal</u> contribution rate for new general members would be approximately 4.0% of payroll. The long term expected annual employer <u>total</u> contribution rate for new general members (includes Group Term Life Insurance and the administrative rate) would be approximately 4.7% of payroll.

For fiscal year 2013, the <u>total</u> contribution rate for new general members (includes Group Term Life Insurance and the administrative rate) would be approximately 7.3% of payroll (7.15% employer share, 0.15% employee share added to 4%, 5%, or 6%). The FY2013 contributions assume that the new tier will be added to the existing ERS plan, and does not become its own, independent plan.

“For ERS members in retirement plans that allow retirement without regard to age, the long term expected and FY 2013 contributions would vary by plan with a representative set of the larger plans given in the table below (with the general plan for tiers 5 and 6 included for reference):

	Long Term Expected Contribution		**FY 2013 Contribution**	
Plan	**Employer**	***Employee**	**Employer**	***Employee**
Tier 5 General	9.4%	3.0%	14.9%	3.0%
Tier 6 General	4.7%	4.00%, 5.00% or 6.00%	7.15%	4.15%, 5.15% or 6.15%
Non-State COs	6.5%	4.00%, 5.00% or 6.00%	8.70%	5.70%, 6.70% or 7.70%
State COs	7.9%	4.90%, 5.90% or 6.90%	10.50%	7.50%, 8.50% or 9.50%
Sheriffs (553)	9.7%	6.70%, 7.70% or 8.70%	13.45%	10.45%, 11.45% or 12.45%
*This is the total employee contribution rate, including that which is based upon pay.				

“Insofar as this bill would affect the New York State and Local Police and Fire Retirement System (PFRS), the significant design changes to the defined benefit plan include:

1. Employee contributions of X+Y% of pay for all years of service, except members enrolled in a plan that limits the amount of creditable service that may be accrued would not be required to contribute after accruing the maximum amount of creditable service under such plan,

where X is determined as follows:

if the annual pay rate is $66,000 or less then X = 4.0%
if the annual pay rate is $66,001 to $132,000 then X = 5.0%
if the annual pay rate is $132,001 or more then X = 6.0%

and Y is determined as follows:

if the plan’s <u>total</u> contribution rate (T) for the fiscal year is greater than 14% then Y = (T – 14%) /2
if the plan’s <u>total</u> contribution rate (T) for the fiscal year is less than 10% then Y = (T – 10%) /2
otherwise Y = 0%

2. Final average salary (FAS) would be based on a 5 year average, with no year’s salary permitted to exceed 8% of the average of the previous 4 year’s salary,
3. Annual overtime paid at a rate greater than the standard rate of pay would not be included in the definition of wages and final average salary,
4. Reportable salary (for a fiscal year) may not exceed the salary of the Governor of the state of New York, which currently is set in law to be $179,000 (the reportable salary would change when the Governor’s salary does),

5. Any form of termination pay and additional compensation paid in anticipation of retirement would no longer be included in a member's final average salary,
6. Members in regular plans (where retirement eligibility requires the attainment of a certain age as well as the accumulation of a certain amount of service credit) must attain age 65 before they may receive a service retirement benefit,
7. Twelve year vesting.
"If this bill is enacted, NYSLRS would calculate new plan rates for all PFRS members who first enter on or after April 1, 2012. For PFRS members in retirement plans that allow retirement without regard to age, the long term expected and FY 2013 contributions would vary by plan with a representative set of the larger plans given in the table below. The FY2013 contributions assume that the new tier will be added to the existing PFRS plan, and does not become its own, independent plan.

	Long Term Expected Contribution		**FY 2013 Contribution**	
Plan	**Employer**	***Employee**	**Employer**	***Employee**
Tier 5 384D	14.8%	3.0%	20.1%	3.0%
Tier 6 384D	10.2%	4.00%, 5.00% or 6.00%	13.8%	4.00%, 5.00% or 6.00%
Tier 5 384E	15.1%	3.0%	20.5%	3.0%
Tier 6 384E	10.6%	4.00%, 5.00% or 6.00%	14.15%	4.15%, 5.15% or 6.15%
T5 State Police	16.2%	3.0%	22.1%	3.0%
T6 State Police	10.9%	4.00%, 5.00% or 6.00%	14.35%	4.35%, 5.35% or 6.35%
*This is the total employee contribution rate, including that which is based upon pay.				

"There would also be additional administrative expenses to inform employers and new members of the new plan provisions and to modify automate systems. Employee contributions would now be a function of base salary, retirement plan and options, and fiscal year, instead of one fixed rate. To implement these employee contribution rate changes the modification of NYSLRS automated systems would be substantial with an associated implementation expense estimated at $3 to 5 million. The more complicated system would be more challenging to maintain, apply, and explain, resulting in estimated annual ongoing expenses in the millions of dollars. The state and each of the approximately 3,000 participating employers would have to modify their methods for withholding employee contributions, which could also lead to total expenses in the millions of dollars. Further, it seems extremely unlikely that such changes could be implemented by April 1, 2012. Lastly, the bill contains no appropriation to support the additional payroll administrative expenses to the Office of the State Comptroller or the implementation and ongoing expenses of NYSLRS related to the new tier.
"This bill would provide new members who first join public retirement systems in New York State on or after April 1, 2012 the option to become covered under the provisions of a new defined contribution plan in lieu of the defined benefit plan.
The significant design features of the defined contribution plan include:
1. Mandatory employer contributions of 4% of wages.

2. Matching employer contributions for voluntary employee contributions of up to 3% of wages.
3. Employee and employer contributions are subject to limits in Federal Law.
4. A death benefit equal to
    - the member's salary after completion of one year of service,
    - two year's salary after completion of two year's service, and
    - three year's salary after completion of three year's service,

    reduced by the employer contributions already made to the employee's defined contribution account.

5. There is no disability benefit.

6. Members may not opt out of the defined contribution plan once they have opted in.
7. The defined contribution plan is to be administered by the New York State and Local Retirement System, which may enter into agreements with qualified providers for investment of member accounts and general administration of the plan.

"Assuming that employees contribute 3% or more to maximize the employer match, the long term expected total annual employer contribution rate for all members who choose the defined contribution plan (includes the death benefit and the ongoing administrative rate) would be approximately 7.7% of payroll.

"There would also be additional NYSLRS administrative expenses to establish the new defined contribution plan. Such expenses would include legal costs to draft and submit plan documents for review by the Internal Revenue Service, drafting and promulgating such rules and regulations as may be necessary or required to implement the defined contribution program, entering into general agreements with qualified providers for the investment of member accounts and general administration of the plan, informing employers and new members of the new plan provisions, and establishing the DC death benefit. These establishment expenses are currently estimated at $3 to 10 million.

"Additionally, the state and participating employers will incur costs to modify their payroll systems and procedures in order to collect employee contributions and remit them along with mandatory employer contributions shortly after each payroll. Such costs are estimated to be $1 million for changes to the state payroll system related to the defined benefit and defined contribution plans. Remittance of employer contributions on a payroll schedule, rather than annually under the defined benefit plan, will affect employers' cash management. It also seems extremely unlikely that such a plan could be implemented by April 1, 2012. Further, the bill contains no appropriation to support the additional payroll administrative expense to the Office of the State Comptroller or the implementation and ongoing expenses of NYSLRS related to the new plan.

"In addition, employees will incur management and investment expenses for their defined contribution accounts estimated to average 0.5% of the account balance annually."

"Summary of relevant resources:

"Data: March 31, 2011 Actuarial Year End File with distributions of membership and other statistics displayed in the 2011 Report of the Actuary and 2011 Comprehensive Annual Financial Report.

"Assumptions and Methods: 2010 and 2011 Annual Report to the Comptroller on Actuarial Assumptions, Codes Rules and Regulations of the State of New York: Audit and Control.

"Market Assets and GASB Disclosures: March 31, 2011 New York State and Local Retirement System Financial Statements and Supplementary Information.

"Valuations of Benefit Liabilities and Actuarial Assets: summarized in the 2011 Actuarial Valuations report.

"I am a member of the American Academy of Actuaries and meet the Qualification Standards to render the actuarial opinion contained herein.

"This estimate, dated February 1, 2012, and intended for use only during the 2012 Legislative Session, is Fiscal Note No. 2012-67, prepared by the Actuary for the ERS and PFRS."