Vermont Legislative Joint Fiscal Office

One Baldwin Street • Montpelier, VT 05633-5701 • (802) 828-2295 • Fax: (802) 828-2483

FISCAL NOTE

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Prepared by: Stephen Klein

H.673 - AN ACT RELATING TO RETIREMENT AND PENSION AMENDMENTS

Supplemental Fiscal Note

The primary fiscal information on this bill is part of the package of materials that has been submitted by the Treasurer. This supplemental fiscal note summarizes impacts in five areas and provides additional issue to consider.

1. **Teachers Retirement Fund**: Since FY 2008, when it was funded at 80.9% of actuarial value, the Teachers Retirement Fund's funding level has experienced a decline:

- 2009 65.4%
- 2010 66.5%
- 2011 63.8%
- 2012 61.6%
- 2013 60.5%

In part, this decline is due to the retired teacher health care costs being paid from the Teachers Retirement Fund (without a dedicated source of revenue for these costs). Under current projections, the FY 2015 actuarial funding shortfall will grow from $28 million (less the $7.55 million added in the budget to address this issue), to $50 million in 2037. Without action, therefore, the level of pension funding will continue to erode.

2. **The General Fund**: The plan envisions the General Fund contributions increasing above current payments for the next four years, as follows:

- FY 2016 $5,000,000 + funds otherwise paid to teachers retirement fund: $2,660,218
- FY 2017 $7,500,000 + funds otherwise paid to teachers retirement fund: $4,273,594
- FY 2018 $10,000,000+ funds otherwise paid to teachers retirement fund: $6,108,212
- FY 2019 Inflation adjusted increases at 3.5% + funds otherwise paid $8,192,984
- The Treasurer projects that these early payments will result in a lower long term General Fund obligation in future years for payments to the Teachers Retirement and this health care Fund.

3. **Interfund Borrowing**: The plan envisions that the General Fund will make up to $30 million in loans from the State's cash flow to capitalize the Retired Teachers Health Care and Medical Benefits Fund. The Treasurer projects a financial benefit to this arrangement by assuming the Retired Teachers Health Care and Medical Benefits Fund will create savings that exceed those of the State's cash flow reserves. Key issues include:

- Vermont cash flow reserves average about $250 million with an average annual low of $200 million.

- In the depths of the recession, the cash flow reserve reached a low of $19.9 million (April 2009).
- Any reduction in cash flow increases the risk of needing to resort to short term borrowing to cover cash flow shortages.
- The repayment of inter-fund borrowing should be done as expeditiously as possible.

4. **School District and Education Fund Impacts**: School districts and the Education Fund will see three areas of impact:

    - First, there will be a new employer assessment in the amount of $1,072 per new teacher hired. The new assessment will apply only to teachers that have not previously been a part of the pension system.
        - The income to the Teachers Retirement Fund from the employer assessment will be paid by the schools and is estimated at:
            - FY 2016 $ 375,000
            - FY 2020 $2,873,165
            - FY 2024 $5,820,583
        - The impact on the Education Fund will be a function of which districts hire new teachers and the extent to which these new costs impact education spending.
        - To the extent that the assessment creates a disincentive to hire new teachers, the upward impact on education spending will be lower.
- Second, districts will have to absorb a full allocation of pension costs for position funded via federal grants (approximately 12.5% of salary). This will reduce ability of grant funds to support other activities.
    - The impact is projected at $3,000,000 in FY 2016, growing at 2% per year
    - It is not easy to estimate the level of activities that will be forgone or funded through other means.
- Third, districts might see an additional pressure on bargaining in that teachers are required to pay an added charge for pension costs (see below).

5. **Teachers**: New teachers will be required to pay a one percent additional contribution to pension funding. This will have three impacts:

- It will raise a projected $1,002,007 million in FY 2015, growing to $2,534,638 by FY 2024.
- It will create a cost to new teachers. This cost could impact the competitive value of positions in Vermont public schools.
- It may create bargaining pressure on school districts to increase wages in response to the increased pension contributions.

6. **Additional Considerations**:

- As Vermont moves to Green Mountain Care, there will be a major reduction in retiree health care liabilities and a change in how these liabilities are financed. The underlying bill calls for a working group to assess those impacts and the resulting changes to the financing system that would be required.
- It is difficult to predict changes in the behavior of schools as a result of this legislation, such as changes to hiring practices and teacher quality.
- Without this funding, continued decline in the funding level of the teacher's retirement system could create pressures on retirement benefits that could affect teacher recruitment and retention.