

Director: Paul Matson

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	FY 2003 Actual	FY 2004 Estimate	FY 2005 Approved
OPERATING BUDGET			
<i>Full Time Equivalent Positions</i>	173.0	197.0	197.0 ^{1/}
Personal Services	7,250,900	7,447,500	7,626,500
Employee Related Expenditures	1,541,200	2,167,800	2,308,600
Professional and Outside Services	4,706,500	3,166,600	3,453,200
Travel - In State	45,300	24,900	24,900
Travel - Out of State	22,200	25,000	25,000
Other Operating Expenditures	1,286,400	1,929,800	1,213,800
Equipment	363,500	124,500	124,500
OPERATING SUBTOTAL	15,216,000	14,886,100	14,776,500
SPECIAL LINE ITEMS			
Information Technology Plan	4,539,700	9,039,600	9,051,900 ^{2/}
AGENCY TOTAL	19,755,700	23,925,700	23,828,400^{3/}

FUND SOURCES

Other Appropriated Funds

Long-Term Disability Administration Account	2,405,500	2,616,800	2,897,700
State Retirement System Administration Account	17,350,200	21,308,900	20,930,700
SUBTOTAL - Other Appropriated Funds	19,755,700	23,925,700	23,828,400
SUBTOTAL - Appropriated Funds	19,755,700	23,925,700	23,828,400
Other Non-Appropriated Funds	21,604,000	22,548,800	22,548,800
TOTAL - ALL SOURCES	41,359,700	46,474,500	46,377,200

AGENCY DESCRIPTION — The Arizona State Retirement System (ASRS) provides retirement, survivors, health and disability benefits to employees of most public employers in Arizona, including public schools, most local and county governments, and the State of Arizona. As of June 30, 2003, ASRS membership included approximately 202,500 active (working and contributing) members, 123,600 inactive members, 66,400 retired members, 4,600 disabled members, and approximately \$18.7 billion in assets (market value).

PERFORMANCE MEASURES	FY 2003 Appropriation	FY 2003 Actual	FY 2004 Appropriation	FY 2005 Appropriation
• % of members satisfied with ASRS telephone services	85	82	87	87
• % of members satisfied with the service purchase process	85	NA	82	82
• % of investment returns	8	2.4	8	8
• % of liability funded	100	100	100	100
• % of benefit payment calculations that are accurate as measured by quality control sample	96	98.45	96	96

Comments: The agency did not submit information for any measure labeled as “NA.”

^{1/} Includes 18 FTE Positions funded from Special Line Items in FY 2005.

^{2/} Before the expenditure of the appropriation of \$9,039,600 in FY 2004 and \$9,051,900 in FY 2005 and the hiring of FTE Positions appropriated for the agency's information technology plan, the Retirement System shall present an expenditure plan in each year to the Joint Legislative Budget Committee Staff for review. The Retirement System shall include the approval of the project investment justification document by the Information Technology Authorization Committee as part of its submission to the Joint Legislative Budget Committee Staff. The agency shall provide semiannual reports to the Joint Legislative Budget Committee Staff regarding the expenditures and project tasks completed to date. Funding appropriated for this purpose is exempt from the provisions of A.R.S. § 35-190, relating to lapsing of appropriations through June 30, 2005. Actual divestiture of monies from the Retirement Fund for expenditure shall occur following the Joint Legislative Budget Committee Staff review of the agency's information technology plan. (General Appropriation Act footnote, as adjusted for statewide allocations)

^{3/} General Appropriation Act funds are appropriated as an Operating Lump Sum with Special Line Items by Agency.

This agency's budget was originally appropriated in Laws 2003, Chapter 262. For details on this agency's FY 2005 budget, please see the *FY 2004 Appropriations Report*. Laws 2004, Chapter 275 amended the budget to incorporate statewide salary changes and other statewide technical adjustments. (Please see the *Statewide Adjustments* section at the end of this *Appropriation Report* for details.)

Additional Legislation

ASRS; Service Purchase; Cost

Laws 2004, Chapter 352 changes the formula used to calculate the cost for ASRS members to purchase credited services to a methodology based on the actuarial present value of the additional benefit. Actuaries estimate that this legislation will result in a 0.30% decrease in the ASRS contribution rate, beginning in FY 2006. Based on current General Fund payroll, this reduction is expected to generate General Fund savings of approximately \$2,485,200 and Other Fund savings of approximately \$1,477,100.

ASRS; Retirement Incentive Costs

Laws 2004, Chapter 106 prohibits participating employers from offering employees an early retirement incentive that generates additional costs to ASRS. If employers choose to offer early retirement incentives, the employer must contribute monies to ASRS to fund the additional benefit liability created by the early retirement incentive. Actuaries estimate that this legislation will result in a 0.11% decrease in the ASRS contribution rate, beginning in FY 2006. Based on current General Fund payroll, this reduction is expected to generate General Fund savings of approximately \$911,200 and Other Fund savings of approximately \$541,600.

PSPRS; Pension Limitation

Laws 2004, Chapter 325 makes several changes to PSPRS statutes, one of which could have an effect on contribution rates in future years. This legislation establishes a new, "catastrophic disability" pension classification that would entitle the member to receive a greater pension if they received a catastrophic injury while on duty. Further, this legislation allows for 10 catastrophic pensions to be awarded in FY 2004, and up to 4 more to be awarded in each subsequent year. Depending on the number of catastrophic pensions awarded, and the distribution of the awards among PSPRS employers, some PSPRS employers could see contribution rate increases in future years. Due to the uncertainty surrounding the total and distribution of the awards, however, actuaries are not able to estimate any potential rate increases.

CORP; Contribution Rate

Laws 2004, Chapter 229 increases the minimum employer contribution rate from 2% to 4% beginning in FY 2006. Further, this legislation establishes that if the average employer contribution rate were to fall below the new 4%

floor, that the employee contribution rate (statutorily set at 8.5%) would be lowered by a corresponding amount. These provisions do not affect the actuarial calculation of the total (employer plus employee) contribution rate, but in future years could increase the employer rate and lower the employee rate by a like amount. Due to rising employer contribution rates, however, actuaries do not expect the conditions to be met in the immediate future. Therefore this legislation is not expected to result in employer rate increases in the short-term.

Other Issues

Actuarial Impact of Retirement Legislation

Currently assets exceed liabilities in 3 of the 4 retirement systems. Further details on each system follows.

ASRS

The FY 2004 contribution was 5.2% and due to the fact that contribution rates are established on a biennial basis, employers and employees are also contributing 5.2% in FY 2005. Subsequent to setting the rate, the fund's financial status declined. While assets exceeded liabilities by \$1 billion at the end of FY 2002, liabilities were greater than assets by \$786 million at the end of FY 2003. If the rate were to be adjusted to reflect fund performance and benefit enhancements enacted in the 2003 Legislative Session, the actual contribution rate would have been 6.96%.

The impact of the legislation enacted in the 2004 Legislative Session would be to reduce the contribution rate by (0.41)% in FY 2006. The actual FY 2006 contribution rate, however, will depend on fund performance during FY 2004 and the "underfunding" of rates during FY 2005.

PSPRS

The average FY 2004 rate for all participating, state and local employers in PSPRS was 7.66%. Subsequent to setting the FY 2004 rates, the fund's performance declined. While assets exceeded liabilities by \$540.2 million at the end of FY 2002, that margin dropped to \$41.8 million by the end of FY 2003. In addition, benefit enhancements enacted in the 2003 Legislative Session were expected to increase the average contribution rate by 0.03%. As a result of fund performance and legislative enactments, the average rate in FY 2005 would be 10.07%. Due to the biennial state budget, participating state employers continue to contribute based on FY 2004 rates. (See the *General Provisions* section of this *Appropriations Report* for more information on contribution rates for participating state agencies.)

There was no legislation passed in the 2004 Legislative Session that affected employer contribution rates. The FY 2006 contribution rates, however, will depend on fund performance during FY 2004 and the "underfunding" of rates in FY 2005. (See page 261 of the *FY 2004*

Appropriations Report for more information on benefit enhancements enacted in the 2003 Legislative Session.)

The above discussion is based on the PSPRS systemwide average employer contribution rate. However, individual PSPRS employers do not contribute the systemwide average, but instead contribute an actuarially determined rate specific to each employer.

CORP

The average FY 2004 rate for all participating, state and local employers in CORP was 3.95%. Subsequent to setting the FY 2004 rates, the fund’s performance declined. While assets exceeded liabilities by \$150.2 million at the end of FY 2002, that margin dropped to \$102.5 million by the end of FY 2003. In addition, benefit enhancements enacted in the 2003 Legislative Session were expected to increase the average contribution rate by 0.02%. As a result of fund performance and legislative enactments, the average rate in FY 2005 would be 4.07%. Due to the biennial state budget, the Arizona Department of Corrections and the Department of Juvenile Corrections continue to contribute based on FY 2004 rates of 4.01% and 5.08%, respectively. There was no legislation passed in the 2004 Legislative Session that affected employer contribution rates. The FY 2006 contribution rates, however, will depend on fund performance during FY 2004 and the “underfunding” of rates in FY 2005. (See page 261 of the FY 2004 Appropriations Report for more information on benefit enhancements enacted in the 2003 Legislative Session.)

The above discussion is based on the CORP systemwide average employer contribution rate. However, individual CORP employers do not contribute the systemwide average, but instead contribute an actuarially determined rate specific to each employer. (See the General Provisions section of this Appropriations Report for more information on contribution rates for participating state agencies.)

EORP

EORP assets exceed liabilities by \$55.6 million. These monies are used to reduce the total amount of court fees needed to cover employer contributions from an average of 21.12% to 14.54% of elected officials’ salaries. EORP receives a fixed percentage of court fees to fund employer contributions, and in previous years these court fees have been large enough to produce a buffer. However, as of FY 2004 court fees are no longer enough to cover employer contributions.

The following table summarizes the impact of the total package of benefit enhancements enacted in the 2004 Legislative Session for each retirement system. (See pages 259-262 of the FY 2004 Appropriations Report for more information on benefit enhancements enacted in the FY 2003 Legislative Session.)

<u>System</u>	<u>Contribution Rate Change</u>	<u>Fiscal Impact Beginning FY 2006 (\$ in Millions)</u>
ASRS	(0.41)%	(3.4) GF (2.0) OF

^{1/} The actual FY 2006 rate will also depend on fund performance and prior 2003 legislative enactments.

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