

Director: Paul Matson

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	FY 2005 Actual	FY 2006 Estimate	FY 2007 Approved
OPERATING BUDGET			
<i>Full Time Equivalent Positions</i>	197.0	221.0	231.0 ^{1/}
Personal Services	7,600,700	8,754,600	9,446,400
Employee Related Expenditures	2,045,400	2,721,500	3,261,100
Professional and Outside Services	3,208,300	3,554,300	3,569,400
Travel - In State	45,400	53,600	53,600
Travel - Out of State	30,100	25,000	25,000
Other Operating Expenditures	1,431,900	1,384,100	1,512,900
Equipment	55,500	235,200	197,500
OPERATING SUBTOTAL	14,417,300	16,728,300	18,065,900
SPECIAL LINE ITEMS			
Information Technology Plan	7,105,900	6,401,600	3,010,100 ^{2/}
Retiree Health Insurance; Rural Subsidy	0	28,000	0
Ch. 309 Optional Forms of Retirement	0	0	50,000
AGENCY TOTAL	21,523,200	23,157,900	21,126,000^{3/4/}
FUND SOURCES			
<u>Other Appropriated Funds</u>			
Long-Term Disability Administration Account	2,456,100	2,897,700	2,897,700
State Retirement System Administration Account	19,067,100	20,260,200	18,228,300
SUBTOTAL - Other Appropriated Funds	21,523,200	23,157,900	21,126,000
SUBTOTAL - Appropriated Funds	21,523,200	23,157,900	21,126,000
Other Non-Appropriated Funds	187,880,800	187,880,800	187,880,800
TOTAL - ALL SOURCES	209,404,000	211,038,700	209,006,800

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 the June 30, 2005 valuation, ASRS membership included approximately 212,202 active (working and contributing) members, 149,768 inactive members, 73,853 retired members, 4,939 disabled members, and approximately \$21.9 billion in assets (market value). Funding for the agency is appropriated except for investment management and consulting fees, rent, actuarial consulting fees, legal counsel costs, retiree payroll and health insurance program administration.

^{1/} Includes 20 FTE Positions funded from Special Line Items in FY 2007.

^{2/} Before the expenditure of the appropriation of \$3,010,100 in FY 2007 and the hiring of FTE Positions appropriated for the agency's information technology plan, the Retirement System shall present an expenditure plan to the Joint Legislative Budget Committee Staff for review. The expenditure plan shall include current year and prior years' appropriations to be spent in the current year and prior year appropriation balances. 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. 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/} The State Retirement System shall provide a report by the end of each calendar quarter during FY 2007 to the Joint Legislative Budget Committee on the discussions and actions of the State Retirement System Board regarding their efforts to minimize the retirement contribution rate. (General Appropriation Act footnote)

^{4/} General Appropriation Act funds are appropriated as an Operating Lump Sum with Special Line Items by Agency.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005	FY 2007
	Actual	Actual	Actual	Approved
<ul style="list-style-type: none"> • % of members satisfied with ASRS telephone services Comments: Customer satisfaction has fallen as average wait times increased to 4 minutes and average call abandonment rates rose to over 30% in FY 2005. Additional call center staff was added for FY 2006. 	82	82	73	87
<ul style="list-style-type: none"> • % of investment returns Comments: ASRS assumes an 8% rate of return for rate calculations. 	2.4	17.5	8.5	8.0
<ul style="list-style-type: none"> • % of benefit payment calculations that are accurate as measured by quality control sample Comments: The agency did not submit information for this measure in FY 2004 or FY 2005. 	98.45	NA	NA	96

Operating Budget

The budget provides \$18,065,900 for the operating budget in FY 2007. This amount consists of:

	<u>FY 2007</u>
State Retirement System Administration Account	\$15,168,200
Long-Term Disability Administration Account	2,897,700

These amounts include an increase of \$949,500 from the State Retirement System Administration Account for statewide adjustments. *(Please see the Statewide Adjustments section at the end of this Appropriations Report for details.)*

One-Time Equipment

The budget provides a decrease of \$(107,700) from the State Retirement System Administration Account in FY 2007 to eliminate one-time equipment costs. These costs were associated with the creation of 16 new FTE Positions in Member Services, Internal Audit and Investment Management in FY 2006.

Financial Services Staffing

The budget provides an increase of \$495,800 and 10 FTE Positions from the State Retirement System Administration Account in FY 2007 for financial services staffing. The positions include 3 accountants and 7 fiscal services specialists for the Membership, Benefit and General Accounting functions in the Financial Services Division. These positions will replace temporary staff and free accountants for more demanding work. Temporary staff will be diverted to more appropriate areas. Of the amount, \$70,000 is for one-time equipment.

Special Line Items

Information Technology Plan

The budget provides \$3,010,100 and 20 FTE Positions from the State Retirement System Administration Account for the Information Technology Plan in FY 2007. These

amounts include an increase of \$105,700 from the State Retirement System Administration Account for statewide adjustments.

Project Completion

The budget provides a decrease of \$(3,452,900) from the State Retirement System Administration Account in FY 2007 for completion of project development and implementation.

One-Time Equipment

The budget provides a decrease of \$(44,300) from the State Retirement System Administration Account in FY 2007 for the elimination of one-time costs associated with 2 FTE Positions and new software and hardware used for Information Technology development projects. FY 2007 is the second year of a 2-year project and includes one-time expenses of \$263,700.

Monies in this line item are appropriated for the development and operation of a \$46.5 million business reengineering information technology (IT) plan. Funding for the development of the IT plan was completed in FY 2006. The FY 2006 Supplemental Budget Bill (Laws 2006, Chapter 316) extended the lapsing date on the amounts appropriated to this line item for FY 2004, FY 2005 and FY 2006 until June 30, 2007. In FY 2005, some issues arose creating a concern that ASRS would be unable to finish the project on-time. These concerns caused the Information Technology Advisory Committee (ITAC) to put the project in a "red" status. ASRS has made progress in returning the project to a "green" on-time, on-budget status, with an expected development completion date in FY 2008. ITAC has currently placed the project in a "yellow" status. Remaining monies in this line mainly fund the operation of the IT plan.

Retiree Health Insurance; Rural Subsidy

The budget provides no funding in FY 2007 for administrative costs associated with the requirements of Laws 2005, Chapter 297.

Eliminate One-Time Appropriation

The budget provides a decrease of \$(28,000) from the State Retirement System Administration Account in FY 2007. Laws 2005, Chapter 297 included a one-time appropriation of \$28,000 from the State Retirement System Administration Account to ASRS in FY 2006. This amount was to implement changes to the retiree health insurance program necessary to continue the rural subsidy for Medicare-eligible rural retirees only, through FY 2007. This program was set to expire June 30, 2005 and originally included all rural retirees.

Ch. 309 ASRS; Optional Forms of Retirement

Laws 2006, Chapter 309 appropriates \$50,000 from the State Retirement System Administration Account in FY 2007. This amount is a one-time appropriation to implement changes to the benefit payment options available to retirees. This chapter limits the number of times a retiree may change the benefit payout option to one.

Additional Legislation

Ch. 12 ASRS; Deferred Retirement; Repeal

Laws 2006, Chapter 12 repealed the Deferred Retirement Option Program (DROP). A DROP allows retirees to receive a lump sum payout upon retirement. This is done by electing to work a defined period past the retirement eligibility point and depositing the benefit payments in an interest bearing account. In return the member continues to work without accruing additional benefits. The DROP was never implemented but actuaries estimate that the elimination of the program will avoid a 30 basis point (0.30%) increase to the ASRS contribution rate that would have occurred if the program were eventually implemented, making the effect of this change a foregone cost, rather than an actual rate decrease.

Ch. 241 CORP; Return to Work

Laws 2006, Chapter 241 allows retired corrections officers to return to work after retirement and continue to receive their retirement benefits. Because the program is limited to members who were retired as of January 1, 2006, the impact on the contribution rate is estimated to be negligible. The bill also contains provisions for a Reverse DROP in the Correctional Officers Retirement Plan (CORP). This program allows a member, upon retirement, to receive a lump sum payment in exchange for a lower ongoing benefit, based on a shorter term of service. Actuaries estimated that this could add up to 30 basis points (0.30%) to the aggregate CORP contribution rate.

Ch. 251 Special Retirement Plans; Amortization

Laws 2006, Chapter 251 increased the maximum allowable amortization period for unfunded liabilities in the Public Safety Personnel Retirement System (PSPRS), the Elected Officials Retirement Plan (EORP), and CORP from 20 years to 30 years. It also increased the minimum

employer contribution rates and requires 50% of excess assets to be put into a reserve fund. In the short term, extending the amortization period is estimated to decrease the aggregate rate in PSPRS by 133 basis points (1.33%), in CORP by 12 basis points (0.12%), and in EORP by 69 basis points (0.69%). In the long run, however, extending the amortization period does decrease the investment earnings by reducing the base assets.

Ch 308 CORP; Membership Expansion

Laws 2006, Chapter 308 allows probation, surveillance and juvenile detention officers in the judiciary to participate in CORP. Currently, these positions are covered under ASRS. The actual retirement contribution rate for these officers will be set by county, and cannot be known at this time. Actuaries were unable to estimate the full cost of this bill, but based on information for Maricopa County only, the bill is expected to be relatively cost neutral.

Ch. 309 ASRS; Optional Forms of Retirement

Laws 2006, Chapter 309 limits the number of times a retiree may change the benefit payout option to one. Prior to this legislation, a retiree could switch back and forth between having a survivor benefit and not having the benefit. With the survivor benefit, the monthly benefit payment is lower, but continues for the beneficiary after the retiree's death. By switching to a survivor benefit in times of ill health, the retiree is more likely to receive the survivor benefit without having to receive the lower monthly benefit for as much time. This legislation limits the ability of the retiree to switch to or from a survivor benefit to one time after the initial benefit election is made. Actuaries estimate that this could decrease the contribution rate by 36 basis points (0.36%).

Table 1 summarizes the contribution rate impacts described in this section.

Table 1	
Legislative Impact on State Retirement System Contribution Rates	
System	Basis Points*
ASRS	
Ch. 12 ASRS; Deferred Retirement; Repeal	(30)
Ch. 309 ASRS; Optional Forms of Retirement	(36)
PSPRS	
Ch. 251 Special Retirement Plans; Amortization	(133)
CORP	
Ch. 241 CORP; Return to Work	30
Ch. 251 Special Retirement Plans; Amortization	(12)
Ch 308 CORP; Membership Expansion	?
EORP	
Ch. 251 Special Retirement Plans; Amortization	(69)

* Each proposal has its own time horizon in terms of when it will affect the retirement rate. As a result, the basis point impacts cannot be added to yield a net change in the retirement rate in the short run.

Other Issues

Retirement System Assets and Funding Levels

Table 2 shows the assets and the funding level (or the degree to which the projected assets meet projected liabilities) for each of the State retirement systems. (Data is as of the FY 2005 year-end valuations.)

<u>System</u>	<u>Assets (\$ in millions)</u>	<u>Funding Level</u>
ASRS	\$21,901	85.3%
PSPRS	\$4,608	82.1%
CORP	\$789	96.4%
EORP	\$311	95.5%