CONSOLIDATED RETIREMENT REPORT

Summary

The Consolidated Retirement Report (CRR) provides financial information on the state's retirement systems, including the state cost, contribution rates, and other related policy and legal issues.

This section includes information on the following:

- FY 2017 Impacts and Total Funding
  - Arizona State Retirement System (ASRS)
  - Public Safety Personnel Retirement System (PSPRS) and Corrections Officer Retirement Plan (CORP)
  - Elected Officials' Retirement Plan (EORP) and Elected Officials' Defined Contribution Retirement System (EODC System)
  - University Optional Retirement Plan (UORP)
- 2016 Session Legislation
  - PSPRS Modifications and Proposition 124
  - Other Bills
- Litigation Issues
  - *Fields v. Elected Officials' Retirement Plan*
  - *Hall v. Elected Officials' Retirement Plan*
- Background
  - The Different Systems
  - Enrollment and Funded Status
  - Permanent Benefit Increase
  - Long-Term Contribution Rate Estimates

FY 2017 Impacts and Total Funding

The General Fund cost associated with all retirement systems in FY 2017 is estimated to be $178.3 million and the Total State Funds cost is $498.5 million. *(Please see Table 1 for the total costs.)*

The employer contribution rate for the retirement systems may change each year depending on the latest actuarial valuation. Some of the retirement costs may be covered by agencies' non-appropriated funding sources. Based on the January JLBC Baseline estimates, the FY 2017 employer contribution will increase for ASRS, PSPRS, and CORP as follows:

- ASRS – A General Fund increase of $58,900 and a Total State Funds increase of $245,800 as a result of a slightly higher FY 2017 ASRS contribution rate. The FY 2017 budget does not adjust agency budgets to account for these cost increases.
- PSPRS – A General Fund increase of $418,600 and a Total State Funds increase of $1.9 million. The budget includes $1.53 million in Other Appropriated Funds in FY 2017 to fund the FY 2017 PSPRS contribution rate increase for the Department of Public Safety (DPS).
- CORP – A General Fund increase of $914,000 and Total State Funds increase of $959,500. The FY 2017 budget includes $723,500 from General Fund in FY 2017 to fund the FY 2017 contribution rate increase in the Arizona Department of Corrections (ADC).
- EORP and the EODC System – Because elected officials' contribution rates are fixed in statute, there would not be an automatic FY 2017 cost increase. EORP actuaries, however, have indicated that current contribution rates will be enough to pay out members' benefits for only 15 more years. *(Please see EORP Funding Options in the FY 2017 JLBC Baseline for more information.)*
- UORP – Because the employer contribution rate is fixed at 7%, there is no change in the FY 2017 employer contribution rate.

Table 2 shows the total budgeted employer cost changes across retirement systems in the FY 2017 budget. The budget appropriates $2.25 million to state agencies for

Table 1

Arizona Public Retirement FY 2017 System Employer Cost

	FY 2017 Change 1/			FY 2017 Total Cost 2/		
	General Fund	**All Other Funds 3/**	**Total**	**General Fund**	**All Other Funds 3/**	**Total**
Arizona State Retirement System	$ 58,900	$ 186,900	$ 245,800	$ 67,633,800	$ 214,544,300	$ 282,178,100
Public Safety Personnel Retirement System	418,600	1,445,600	1,864,200	19,423,200	61,189,200	80,612,400
Corrections Officer Retirement Plan	914,000	45,500	959,500	69,994,400	941,700	70,936,100
Elected Officials' Retirement Plan/Elected Officials' Defined Contribution Retirement System	-	-	-	7,938,100	109,900	8,048,000
University Optional Retirement Plan	-	-	-	13,272,000	43,469,000	56,741,000
Grand Total	**$ 1,391,500**	**$ 1,678,000**	**$ 3,069,500**	**$ 178,261,500**	**$ 320,254,100**	**$ 498,515,600**

1/ Represents the cost of the change in the employer contribution rate increase for all state agencies.
2/ Represents the JLBC estimate of the total cost of the system and does not reflect FY 2017 change in Personal Services costs.
3/ Includes both Other Appropriated Funds and Non-Appropriated Funds.

the FY 2017 rate increases discussed above, and an additional $2.76 million for FY 2016 rate increases, for a total of $5.0 million. The FY 2017 budgeted employer cost change is significantly lower than the $27.4 million for employer retirement cost changes included in the FY 2016 budget because the FY 2016 rate increase reflected the increase in unfunded liabilities resulting from the court ruling in the *Fields* case. *(Please see Litigation section for additional information.)*

Table 2

FY 2017 Budgeted Employer Cost Change

	FY 2016 Rate Increase	FY 2017 Rate Increase	Total
PSPRS			
General Fund	0	0	0
Other Appropriated Funds	1,814,300	1,528,500	3,342,800
Subtotal	**$ 1,814,300**	**$ 1,528,500**	**$ 3,342,800**
CORP			
General Fund	947,700	723,500	1,671,200
Other Appropriated Funds	0	0	0
Subtotal	**$ 947,700**	**$ 723,500**	**$ 1,671,200**
Total			
General Fund	947,700	723,500	1,671,200
Other Appropriated Funds	1,814,300	1,528,500	3,342,800
Grand Total	**$ 2,762,000**	**$ 2,252,000**	**$ 5,014,000**

The following sections discuss FY 2017 contribution rates for the state's retirement systems and the fiscal impacts associated with those rates. Legal issues that affect the state's retirement systems are discussed at the end of the CRR.

ASRS

The General Fund cost associated with ASRS in FY 2017 is estimated to be $67.6 million and the Total State Funds cost is $282.2 million.

At its December 2015 meeting, the ASRS Board of Trustees decreased the system's employer contribution rate (0.01)%, from 11.35% of Personal Services in FY 2016 to 11.34% in FY 2017. This reduction is offset by a 0.02% increase in a separate rate for disability insurance. The employer contribution rate for disability insurance will increase from 0.12% to 0.14%, for a total overall employer contribution rate of 11.48%, an increase of 0.01%. This higher contribution rate increases the General Fund cost by $58,900 and the Total State Funds cost by $245,800 in FY 2017. The FY 2017 budget does not increase agency budgets for these costs. *(Please see Table 3 for historical ASRS contribution rates, excluding disability.)*

The rate for disability insurance increased because of increased liabilities from individuals not recovering and coming off disability as anticipated and subpar asset performance.

(Please see Table 5 for reasons behind contribution rate changes and Fields v. Elected Officials' Retirement Plan section for more information on the case.)

Table 3

ASRS Contribution Rates
(Excludes Disability)

Fiscal Year		Rate 1/	Fiscal Year	Rate 1/
FY 1983		7.00	FY 2001	2.17
FY 1984		7.00	FY 2002	2.00
FY 1985		6.27	FY 2003	2.00
FY 1986		5.67	FY 2004	5.20
FY 1987		5.53	FY 2005	5.20
FY 1988		4.00	FY 2006	6.90
FY 1989	2/	4.78	FY 2007	8.60
FY 1990	2/	1.29	FY 2008	9.10
FY 1991	2/	3.37	FY 2009	8.95
FY 1992	2/	3.17	FY 2010	9.00
FY 1993	2/	3.10	FY 2011	9.60
FY 1994	2/	2.65	FY 2012	10.50
FY 1995	2/	3.26	FY 2013	10.90
FY 1996		3.36	FY 2014	11.30
FY 1997		3.20	FY 2015	11.48
FY 1998		3.05	FY 2016	11.35
FY 1999		2.85	FY 2017	11.34
FY 2000		2.17		

1/ As a percent of salary, employee and employer each pay this rate except for FY 2012, when employers paid 9.87% and employees 11.13%. This non-50/50 split was repealed by Laws 2012, Chapter 304, which refunded excess contributions to employees.

2/ Long Term Disability not broken out of the contribution rate from FY 1989 - FY 1995. Rates for these years reflect amounts estimated to be attributable solely to retirement component.

PSPRS and CORP

The General Fund cost associated with PSPRS in FY 2017 is estimated to be $19.4 million and the Total State Funds cost is $80.6 million. In addition, the General Fund cost associated with CORP is $70.0 million in FY 2017 and the Total State Funds cost is $70.9 million.

As a result of the court decision in *Fields v. Elected Officials' Retirement Plan* that overturned portions of the 2011 pension changes (Laws 2011, Chapter 357), the FY 2016 employer contribution rate for PSPRS and CORP increased significantly.

To diminish the immediate fiscal impact of the projected contribution rate increases in PSPRS and CORP, the PSPRS Board of Trustees adopted a policy in 2014 that allowed employers to choose to pay the full contribution amount immediately (which includes the impact of the *Fields* ruling) or a reduced rate that gradually increases to the actuarial rate by FY 2018. The FY 2016 budget assumed all affected state employer groups would pay the full rate and provided $17.8 million from the General Fund in added funding to cover the full contribution rate increase for the Department of Public Safety (DPS) and the Arizona Department of Corrections (ADC).

The projected FY 2017 employer contribution rate for PSPRS and CORP will also increase but the growth would be significantly lower than that of FY 2016. The FY 2017 rate increases for PSPRS and CORP are a result of asset losses and lower-than-estimated employee payroll growth. These variables are partially offset by decreases associated with not having a permanent benefit increase (PBI) this year given the low return on investments and more PSPRS and CORP members being subject to the 2011 pension changes (i.e., Tier 2), who have a less costly tier of benefits.

The budget includes the following funding for FY 2017 contribution rate increases for state agencies with employees enrolled in PSPRS or CORP:

- $1,528,500 from Other Appropriated Funds for PSPRS rate increases for Department of Public Safety employees.
- $723,500 from the General Fund for an increase in the employer contribution rate to CORP for the Arizona Department of Corrections (ADC).

The budget also includes the following increases associated with FY 2016 rate increases in PSPRS and CORP:

- $1,752,000 from the Game and Fish Fund for the Game and Fish Department in FY 2016. This amount funds the costs associated with a 21.78% increase in the PSPRS contribution rate for Game and Fish wardens.
- $62,300 in from the Liquor Licenses Fund in FY 2017 for the Department of Liquor Licenses and Control. This amount funds an 18.06% increase in the PSPRS contribution rate increase for liquor license investigators.
- $947,700 from the General Fund in FY 2017 for the Judiciary. This amount funds a 3.83% CORP contribution rate increase for state-funded probation officers outside of Maricopa County.

PSPRS – The retirement system consists of numerous state and local subgroups, each with its own contribution rate *(see Table 4)*. The aggregate employer rate increases from 41.37% to 42.61%, or 1.24%, if all subgroups used the full rather than the reduced contribution. Compared to employers, the aggregate employee contribution rate remains flat at 11.65%. In addition, only employers pay 1.92% for supplemental disability insurance, an increase of 0.02% from FY 2016.

Table 4

PSPRS/CORP State Employer Group Retirement Rates (Excludes Supplemental Disability)

Retirement System	Employer FY 2016	Employer FY 2017	Employee FY 2017 1/
Public Safety Personnel Ret. System			
Liquor License Investigators	69.19	78.18	11.65
Department of Public Safety 2/	81.00	82.96	6.65
Northern Arizona University Police	48.83	52.13	11.65
University of Arizona Police	33.86	35.00	11.65
Arizona State University Police	35.31	34.20	11.65
Game and Fish Department	88.56	93.17	11.65
Attorney General Investigators	70.46	66.09	11.65
DEMA Firefighters	31.34	28.20	11.65
Parks Police	42.85	44.72	11.65
Corrections Officer Ret. Plan			
Corrections Officer - ADC	18.54	18.74	8.41
Corrections Officer - DJC	22.95	24.86	8.41
DPS Dispatchers 3/	17.62	19.87	7.96
Probation Officers	19.95	20.08	8.41

1/ The PSPRS and CORP employee contributions are unchanged from FY 2016.
2/ The displayed rates reflect that 5% of the DPS member contribution is paid by the state.
3/ Dispatchers hired after November 24, 2009 are ASRS members.

CORP – As with PSPRS, CORP consists of subgroups. The FY 2017 CORP aggregate rate is 18.71%, an increase of 0.50% from FY 2016. The employee contribution rate remains flat at 8.40%. CORP employers also pay 0.27% for supplemental disability insurance, an increase of 0.02% from FY 2016.

(Please see Table 1 for the state costs of contribution rate increases, Table 5 for reasons for change in the contribution rates by system.)

Table 5

Reasons for Change in the Employer Contribution Rate 1/

	ASRS	PSPRS	CORP
FY 2016 Contribution Rate	11.47%	41.37%	18.21%
Asset (Gain)/Loss	-0.01%	0.94%	0.51%
Payroll	0.00%	0.79%	0.32%
Long Term Disability Rate Change	0.02%	N/A	N/A
Tier 2 Employee Benefits	0.00%	-0.17%	-0.16%
Permanent Benefit Increase Effect	0.00%	-0.44%	-0.24%
Other	0.00%	0.12%	0.07%
FY 2017 Contribution Rate	**11.48%**	**42.61%**	**18.71%**
Net Change	**0.01%**	**1.24%**	**0.50%**

1/ Represents aggregate information for PSPRS and CORP. These 2 systems consist of separate employer groups. Each group has its own actuarial status. As a result, the contribution rates may vary for each employer group.

EORP and EODC System

The General Fund cost associated with EORP and the EODC System in FY 2017 is estimated to be $7.9 million and the Total State Funds cost is $8.0 million. These amounts exclude court fees used to offset the cost of the system, as those fees are now deposited directly into the EORP Trust Fund.

As part of closing EORP and establishing the EODC System, A.R.S. § 38-810 established a fixed employer contribution rate of 23.5% for members of both systems, effective January 1, 2014. The employer contribution rate for EORP members goes entirely to the EORP Fund, whereas only 17.5% of the EODC System employer contribution rate goes to the EORP Fund. The remaining 6% of the EODC System contribution rate is deposited into the individual employees' retirement investment account.

The $7.9 million General Fund cost consists of both employer contribution rates and an annual General Fund deposit. The fixed 23.5% EORP and EODC System employer contributions to the EORP Fund are scheduled to continue until FY 2044. The $5.0 million annual General Fund deposit into the EORP Fund is scheduled to continue until FY 2043.

Given fixed contributions, employer costs will not increase in FY 2017.

EORP Funding Options

These current contributions and deposit amounts do not account for the increase in EORP's total actuarial liability following the outcome of *Fields*. Plan actuaries estimate that given current funding levels, the closed EORP will have enough assets to pay member benefits for only the next 15 years. In order to extend this 15-year period and ensure payment of all benefits, the plan actuaries provide 4 possible 30-year funding options for EORP. *(Please see the FY 2017 JLBC Baseline for more details on these options.)*

UORP

The General Fund cost associated with UORP in FY 2017 is estimated to be $13.3 million and the Total State Funds cost is $56.7 million.

While some university employees are members of ASRS, others participate in the optional retirement plan. In this latter plan, employees and their employers each contribute 7% of the employee's gross earnings, which is then invested by the employee. These contribution rates are fixed in statute and do not change in FY 2017.

(Please see Table 6 for projected contribution rates for all systems through FY 2019.)

2016 Session Legislation

The retirement systems were affected by legislation relating to the following issues in the 2016 Regular Session:

PSPRS Modifications and Proposition 124

Laws 2016, Chapter 2 makes numerous changes to PSPRS pension benefits. The sections below discuss Proposition 124 and the repeal of Permanent Benefit Increase (PBI) mechanism, modifications to the Defined-Benefit plan for future PSPRS members, the creation of a new PSPRS defined contribution plan, and the potential fiscal impact of these changes.

PBI Repeal

Prior to Chapter 2, annual increases in the base pension benefit for PSPRS members were funded by a PBI mechanism that determined pension benefit increases based on the availability of excess investment earnings, with increases capped at 4% annually. Chapter 2 replaces the PBI with an annual cost-of-living adjustment (COLA) based on the average annual change in the Phoenix-Mesa Consumer Price Index, capped at 2% annually.

The replacement of the PBI with the COLA could reduce benefit increases for current PSPRS members. As a result, the Legislature adopted SCR 1019, which referred a measure to the ballot that included an amendment to Article XXIX, Section 1 of the Arizona Constitution specifying an exception to the provision that public retirement system benefits not be "diminished or impaired" to permit the changes enacted in Chapter 2. The ballot measure, known as Proposition 124, was approved by voters in the May 2016 special election.

Defined-Benefit Changes

Chapter 2 also modified the base defined-benefit pension for PSPRS members, but only for members hired on or after July 1, 2017 (i.e. Tier 3). These modifications for Tier 3 members include:

- A cap on annual pension compensation of $110,000, adjusted once every 3 years based on an index of public safety wages. For employees hired before July 1, 2017, the annual compensation cap is $265,000, and is adjusted annually by the Internal Revenue Service.
- Employee contributions equal to 50% of 1) the normal cost and 2) unfunded accrued actuarial liabilities solely attributable to Tier 3 members. The employee contribution rate for employees hired before July 1, 2017 is capped by law at 11.65%.
- Annual benefit increases based on the average annual change in the Phoenix-Mesa Consumer Price

Index, capped at 2% annually. The maximum allowable increase is lower than 2% if the funded ratio for the benefits of Tier 3 members falls below 90%, and no increase is allowed if the funded ratio falls below 70%. The aggregate annual benefit increase for employees hired before July 1, 2017 under the PBI mechanism was 4%.
- A minimum normal retirement age of 55. The current retirement age is 52.5 for members hired on or after January 1, 2012 but before July 1, 2017 (Tier 2 employees), and there is no minimum age for members hired before January 1, 2012 for members with at least 20 years of credited service.

Within 90 days of beginning employment, Tier 3 PSPRS members will be required to make an irrevocable choice to enroll in the modified defined-benefit plan or the defined-contribution plan discussed below.

Defined Contribution Plan and Hybrid Plan
Chapter 2 allows Tier 3 employees to enroll in a new PSPRS defined contribution (DC) plan instead of the modified defined-benefit pension plan. The DC plan requires participating employees to contribute 9% of their compensation into a 401(k)-style annuity account each year, with a matching 9% employer contribution.

The employer contributions vest at a rate of 10% per year, resulting in employer contributions and investment earnings being fully vested after 10 years. Vesting determines the share of employer contributions and investment earnings that the employee retains after terminating employment with his or her employer.

Tier 3 employees with employers that do not participate in the federal Social Security program are also allowed to enroll in a hybrid plan. The hybrid plan combines the Tier 3 defined benefit plan with a DC plan that includes a contribution equal to 3% of compensation from both the employer and the employee, subject to the same vesting provisions as the full DC plan.

Proposition 124 also resulted in the enactment of a provision in Chapter 2 that allows Tier 2 employees (i.e., employees hired on or after January 1, 2012, but before July 1, 2017) with an employer that does not participate in Social Security to add the DC plan to their defined benefit pension. Employers with Tier 2 employees who choose to opt into the DC benefit plan are required to contribute 4% of compensation instead of 3% to the annuity account for a specified number of years depending on the employee's date of hire. These temporary extra contributions by employers are intended to allow Tier 2 members to "catch up" to Tier 3 members in the hybrid plan, as Tier 2 members did not have the choice of a DC plan when they initially enrolled in PSPRS.

Fiscal Impact
The plan actuaries project that employer contribution rates in the first year of plan implementation will be 51.0%. This rate is lower than the projected 52.7% employer contribution rate if the *Hall* case results in additional provisions of Chapter 357 being overturned, but is higher than the 45.2% employer contribution rate if Chapter 357 is upheld. As a result, whether Chapter 2 results in savings for PSPRS employers in the short term depends on the outcome of the *Hall* case *(see Hall discussion below).*

Based on these employer contribution rate projections, the JLBC Staff estimates that if *Hall* overturns Chapter 357, Chapter 2 and Proposition 124 would result in savings for state and local employers of $(26.8) million in FY 2018. If Chapter 357 is upheld, the cost to state and local employers is estimated to be $91.4 million.

The primary reason for the difference in the 2 scenarios is related to the COLA created by Chapter 2 for current PSPRS members. The actuaries project that the COLA would provide higher average annual benefit increases than the Chapter 357 PBI for active PSPRS members, which only provides benefit increases if investment returns exceed 10.5% and if the funded status of the PSPRS Trust Fund is at least 60%.

Regardless of the outcome of *Hall,* the actuaries project that Chapter 2 will result in lower employer contribution rates over the long term. The estimated normal cost of benefits for Tier 3 enrollees is 9.8%, compared to 13.2% for employees hired on or after January 1, 2012. Based on these contribution rates, the JLBC Staff estimates that Chapter 2 will result in savings for state and local employers of $(85.4) million in FY 2042.

However, due to the magnitude of PSPRS' current unfunded liabilities, the employer contribution rates are likely to far exceed the normal cost requirement for many years. The actuaries expect that aggregate PSPRS employer contribution rates will exceed 40% until at least 2030.

CORP Reverse Deferred Retirement Option Plan
Laws 2016, Chapter 74 permanently repeals a provision that would have resulted in the expiration on June 30, 2016 of the option for CORP members to voluntarily enroll in a reverse deferred retirement option plan (DROP). The reverse DROP plan allows CORP members with at least 24 years of credited service to receive a lump sum benefit on their date of retirement in addition to a

normal pension benefit. CORP members enrolled in DROP may continue working for up to 5 years once they enroll in the program.

Credit for Military Service

Laws 2016, Chapter 90 reduces the minimum period of military service from 10 years to 5 years for which members of PSPRS, CORP, or EORP may purchase credited service for periods of active military service. The bill also retroactively requires that from and after August 1, 2012, the discount rate used to calculate the benefits purchased for periods of military service shall be equal to the assumed rate of return on investments by the PSPRS Board of Trustees. From and after July 1, 2017, the discount rate shall be equal to the return of 10-year treasury notes plus 2%. The higher discount rate for service purchased before July 1, 2017 will temporarily reduce the cost of service purchases for veterans.

ASRS Eligible Rollovers

Laws 2016, Chapter 96 prohibits ASRS members from using distributions from Individual Retirement Accounts (IRA) to purchase credited service (i.e. indirect rollovers). Members may continue to use rollovers from retirement plans (i.e. direct rollovers) or direct transfers of retirement distributions from financial institutions to ASRS (i.e. Trustee-to-Trustee Transfers) to purchase credited service. Because the Internal Revenue Service (IRS) only withholds taxes for indirect rollovers, the taxes owed on service credit that is purchased using IRA distributions are sometimes reported incorrectly. The bill is intended to reduce reporting errors in the service purchase process.

Private Equity Fee Reporting

The FY 2017 Government Budget Reconciliation Bill (Laws 2016, Chapter 121) requires the ASRS Board of Trustees and the PSPRS Board of Trustees to include in their Comprehensive Annual Financial Reports an estimate of aggregate fees paid for private equity investments, including management fees and performance fees. This reporting requirement is intended to ensure consistent reporting of private equity fees across the retirement systems.

Public Safety Cancer Insurance Program

Laws 2016, Chapter 178 makes changes to the Firefighter, Peace Officer, and Corrections Officer Cancer Insurance program. Previously, only corrections officers and detention officers had the option of enrolling. Chapter 178 renames the program as the "Public Safety Cancer Insurance Program," and extends eligibility for the voluntary cancer insurance program to all CORP members with a participating employer. This would include health care staff, parole officers, food services staff, and correctional employees eligible for CORP.

The bill also allows DPS to establish a voluntary cancer insurance program for CORP employees. Previously, only ADC, the Department of Juvenile Corrections, and local government employers were permitted to establish a voluntary cancer insurance program.

The Cancer Insurance program is a multiple employer group cancer insurance policy for active and retired firefighters, peace officers, and corrections employees administered by the PSPRS Board of Trustees. The policy covers medical treatments and out-of-pocket expenses for cancer that are not covered by health insurance, and has a maximum lifetime benefit of $100,000. Statute caps the annual premium per employee at $180 annually. The current premium is $50.

The program is mandatory for firefighters and peace officers. Employers with a voluntary program must collect premiums from participating employees, and remit those payments to the PSPRS Board of Trustees.

Litigation Issues

Two recent court cases have a significant impact on PSPRS, CORP, and EORP.

Fields v. Elected Officials' Retirement Plan

Laws 2011, Chapter 357 made numerous changes to these systems. Among these changes were reducing PBIs and increasing employee contribution rates. *(Please see the Background section for more discussion of PBIs.)*

The Arizona Supreme Court ruled in *Fields v. Elected Officials' Retirement Plan*, however, that the reduction of PBIs for current retirees violated Article 29 of the Arizona Constitution, which specifies that "public retirement system benefits shall not be diminished or impaired." This ruling also applied to PSPRS and CORP retirees.

PSPRS staff estimates that the *Fields* ruling has increased unfunded liabilities for all systems by $1.8 billion. The increased liabilities in PSPRS and CORP would be paid off over a fixed period of 22 years through an increase in employer contribution rates. When the EORP was closed, the fixed General Fund deposit and contribution rate assumed unfunded liabilities would be paid off by 2044. Because of the increased liabilities in EORP, those amounts may need to be adjusted to account for the fiscal impact of the *Fields* ruling.

Hall v. Elected Officials' Retirement Plan

In addition to *Fields*, there is other ongoing litigation challenging provisions of Chapter 357, which may result in more costs to non-ASRS pension systems. Among other issues, the plaintiffs in *Hall vs. The Elected Officials' Retirement Plan* are litigating the increased contribution rates for members who were active prior to the enactment of Chapter 357. Chapter 357 raised the contribution rates for active members of CORP, EORP, and PSPRS. In EORP (the defendant in the *Hall* case), the contribution rate gradually increased each year from 7% in FY 2011 to 13% in FY 2015. The pre-Chapter 357 employee contribution rates (7%) were fixed in statute. The plaintiffs argued that those statutory rates reflected a contractual agreement that could not be modified without employee consent.

Because the *Fields* decision regarding PBIs only applies to current retirees, the plaintiffs in *Hall*, who are current employees, are also challenging the Chapter 357 PBI structure. The plaintiffs argue that as active members of EORP prior to the enactment of Chapter 357, their benefits may not be "diminished or impaired." If the plaintiffs prevail in *Hall*, the additional fiscal impact of the court case would be lower in today's dollars than *Fields*, mainly because the ruling would reinstate PBIs for some active members who will not retire for many years.

PSPRS staff reports that if EORP loses the *Hall* case, then the case would likely apply to all PSPRS systems (PSPRS/CORP/EORP). PSPRS staff estimated in early 2015 that an adverse ruling in the *Hall* case would increase unfunded liabilities for all systems by $1.3 billion. This additional liability would result in increased employer contribution rates in the fiscal year following the court decision.

In July 2013, the Maricopa County Superior Court ruled against EORP and decided that Chapter 357 applies only to members of EORP who joined the system after the enactment of Chapter 357. The ruling effectively blocks PBI changes from being applied to active members hired before Chapter 357. The ruling was appealed to the Arizona Court of Appeals in March 2015.

In June 2015, the Supreme Court agreed to transfer the case from the Court of Appeals and hear the case. All 5 justices recused themselves (given that they are members of EORP and would be affected by the ruling), however, and appointed a 5-person panel of lower-court judges who are not members of EORP. This panel heard oral arguments from the parties in February 2016.
If the panel rules against EORP, then more active members in other systems (PSPRS and CORP) may also not be subject to Chapter 357. The panel's decision will not be appealable.

Background

The Different Systems

Most public employers in Arizona use 2 retirement systems: ASRS and PSPRS.

- ASRS provides retirement, survivors, health, and disability benefits to employees of most public employers, including public schools, most local and county governments, and the State of Arizona.
- PSPRS provides similar benefits to public employees who work in a public safety capacity, such as law enforcement officials and firefighters.
- In addition, PSPRS staff administers CORP and EORP, which provide the same benefits as PSPRS to specified populations at the state and local levels. EORP is now closed to new enrollees. Elected officials who are elected after January 1, 2014 will be enrolled in the EODC System.

Some university employees are eligible to choose between ASRS or UORP. Unlike ASRS, UORP is a defined contribution plan where the employee and employer each contribute 7% of gross earnings, which is then invested by the employee. The retirement benefits depend on the performance of those chosen investments.

Enrollment and Funded Status

As of June 30, 2015, there were 610,112 active, inactive, retired, and Deferred Retirement Option Plan (DROP) members enrolled in ASRS, PSPRS, CORP, and EORP. Most employees (91%) are enrolled in ASRS. *(Please see Table 7 for more information.)*

Table 7 also shows each plan's assets and liabilities. To calculate the unfunded liability of each plan, actuaries use a modified amount for asset values to reflect certain plan assumptions. *Table 7* reflects current market values for assets and not the actuarial value. The funded status, or the amount of actuarial assets relative to the amount liabilities, of each plan is:

- 77.1% for ASRS;
- 49.0% for PSPRS;
- 57.3% for CORP; and
- 38.8% for EORP.

The above percentages exclude the retiree health portion of the pension plan.

Permanent Benefit Increase

PBIs are increases to a retiree's base benefit. They are dependent on pension performance and a number of other factors. PBIs are not tied to a cost of living index.

The *Fields* ruling reinstituted the pre-Chapter 357 PBI mechanism, which requires that whenever the annual investment earnings from the fund exceed 9.0%, then half of those annual excess earnings are transferred to a PBI reserve account. The ruling applied to any individuals retiring prior to the enactment of Chapter 357. The transfer to the reserve account occurs regardless of the system's overall funded status.

PSPRS actuaries then determine the present value of the reserve account and the monthly benefit increase that the account balance can fund. The annual PBI is then provided in that amount up to a 4% increase. If after a 4% increase monies remain in the reserve account, then those monies would be available for the following year's PBI calculation.

Chapter 357 modifies the PBI structure for PSPRS, CORP, and EORP for members hired after the enactment of Chapter 357. This law allows for a PBI only if the fund has annual investment earnings in excess of 10.5% and the overall funded status is at least 60%. The amount of the PBI would be between 2% and 4%, depending on the funded status of the plan. Chapter 357 would have limited the PBI to the amount of earnings in the fund that exceed 10.5%. Any excess earning amount that was not used for a PBI in a given year would revert back to the fund balance instead of remaining in a separate account.

Laws 2016, Chapter 2 repeals the pre-Chapter 357 PBI mechanism as well as the Chapter 357 PBI mechanism for all members of PSPRS, and replaces it for all members with an annual cost-of-living adjustment (COLA) linked to the Phoenix-Mesa Consumer Price Index. The COLA will be capped at 2% annually. Members of CORP and EORP will continue to have their benefit increases funded based on the PBI mechanism. *(Please see 2016 Session Legislation for additional information.)*

Long-Term Contribution Rate Estimates

A.R.S. § 38-848 requires PSPRS to annually report on estimated contribution rates for the next 10 fiscal years. These estimates are required to include both aggregate rates for PSPRS and CORP, in addition to rates for each state employer group within those systems. *(Please see Table 8 for more information.)*

Table 6

Arizona Public Retirement System Contribution Rate Data 1/

	FY 2016			FY 2017			FY 2018			FY 2019		
	Employer	Employee	Total	Employer	Employee	Total	Employer	Employee	Total	Employer	Employee	Total
ASRS 2/3/	11.47%	11.47%	**22.94%**	11.48%	11.48%	**22.96%**	11.47%	11.47%	**22.94%**	11.59%	11.59%	**23.18%**
PSPRS 4/5/	41.37%	11.65%	**53.02%**	42.61%	11.65%	**54.26%**	42.46%	11.65%	**54.11%**	42.59%	11.65%	**54.24%**
CORP 4/5/	18.21%	8.41%	**26.62%**	18.71%	8.41%	**27.12%**	18.34%	8.41%	**26.75%**	18.25%	8.41%	**26.66%**
EORP 6/	23.50%	13.00%	**36.50%**	23.50%	13.00%	**36.50%**	23.50%	13.00%	**36.50%**	23.50%	13.00%	**36.50%**
EODC 6/	6.00%	8.00%	**14.00%**	6.00%	8.00%	**14.00%**	6.00%	8.00%	**14.00%**	6.00%	8.00%	**14.00%**
UORP 7/	7.00%	7.00%	**14.00%**	7.00%	7.00%	**14.00%**	7.00%	7.00%	**14.00%**	7.00%	7.00%	**14.00%**

1/ This table represents the full FY 2017 contribution rate and does not reflect the phase-in option for CORP and PSPRS. The rates for FY 2016 and FY 2017 are based on the valuation data from 2 years' prior (i.e., FY 2014 and FY 2015). The projected rates for FY 2018 and FY 2019 are based on FY 2015 valuation data.
2/ The ASRS contribution rate for each year includes the contribution rate for long term disability, which is split evenly between the employer and employee.
3/ The ASRS contribution rate for each year assumes no growth in the system population.
4/ The contribution rates for PSPRS and CORP are aggregated. These 2 systems consist of separate employer groups. Each group has its own actuarial status. As a result, the contribution rates may vary for each employer group. *(Please see Table 4 for individual state employer groups.)*
5/ The employer contribution rates displayed for years FY 2018 and FY 2019 exclude the contribution rate associated with retiree health in PSPRS and CORP. This amount, however, is expected to be minimal in each year (approximately 0.25%). Additionally, the employer contribution rates for all years displayed exclude the contribution rate associated with supplemental long term disability insurance (in FY 2017, that rate is 0.27%).
6/ Laws 2013, Chapter 217 established a fixed employer contribution rate for EORP and EODC System members of 23.5% that began January 1, 2014. Of the contribution rate for EODC System members, 6% is retained by the defined contribution system as an employer contribution to the member account and the remaining 17.5% is paid to the EORP Fund.
7/ A.R.S. § 15-1628 fixes the employer and employee contribution rates at 7%.

Table 7

Arizona Public Retirement System Valuation Data as of June 30

	ASRS		PSPRS		CORP		EORP	
Membership								
	FY 2014	**FY 2015**	**FY 2014**	**FY 2015**	**FY 2014**	**FY 2015**	**FY 2014**	**FY 2015**
Active (working and contributing)	203,201	203,252	18,526	18,409	14,595	14,184	843	738
State Active Members	*25,992*	*26,105*	*1,348*	*1,351*	*8,699*	*8,539*	*114*	*97*
Other Active Members 1/	*177,209*	*177,147*	*17,178*	*17,058*	*5,896*	*5,645*	*729*	*641*
Inactive	215,325	219,346	1,563	1,923	1,687	2,318	149	171
Retired Members and Survivor Beneficiaries	126,255	131,536	10,524	11,034	4,090	4,410	1,053	1,116
Deferred Retirement Option Plan	N/A	N/A	1,559	1,675	N/A	N/A	N/A	N/A
Total	**544,781**	**554,134**	**32,172**	**33,041**	**20,372**	**20,912**	**2,045**	**2,025**
Funding Status (dollar values in millions) 2/								
	June 30, 2014	**June 30, 2015**	**June 30, 2014**	**June 30, 2015**	**June 30, 2014**	**June 30, 2015**	**June 30, 2014**	**June 30, 2015**
Market Value of Assets	$35,159	$35,116	$5,936	$6,076	$1,497	$1,540	$314	$309
Total Actuarial Liability	$42,826	$44,574	$12,233	$12,686	$2,638	$2,740	$796	$813
Unfunded Actuarial Liability 3/	$9,904	$10,014	$6,214	$6,468	$1,126	$1,169	$483	$498
Funded Status 3/	76.3%	77.1%	49.2%	49.0%	57.3%	57.3%	39.4%	38.8%

1/ Includes city, county, political subdivision, higher education and other education active members.

2/ Represents aggregate information for PSPRS and CORP. These 2 systems consist of separate employer groups. Each group has its own actuarial status. As a result, the funded status may vary for each employer group.

3/ Calculated on actuarial, not market, value of assets. Excludes the funded status of the retiree health portion of the plan.

Table 8

Arizona Public Retirement System Contribution Rate Historical and Trend Data (Full Rate)

	Actual							Projected								
	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
ASRS																
Employer	9.85%	10.74%	11.14%	11.54%	11.60%	11.47%	11.48%	11.47%	11.59%	10.96%	11.03%	10.63%	10.42%	10.16%	9.95%	9.92%
Employee	9.85%	10.74%	11.14%	11.54%	11.60%	11.47%	11.48%	11.47%	11.59%	10.96%	11.03%	10.63%	10.42%	10.16%	9.95%	9.92%
Total 1/	**19.70%**	**21.48%**	**22.28%**	**23.08%**	**23.20%**	**22.94%**	**22.96%**	**22.94%**	**23.18%**	**21.92%**	**22.06%**	**21.26%**	**20.84%**	**20.32%**	**19.90%**	**19.84%**
PSPRS																
Employer 2/3/	20.89%	22.68%	27.18%	30.44%	32.54%	41.37%	42.61%	42.46%	42.59%	42.92%	42.89%	42.93%	43.11%	43.09%	43.01%	42.91%
Employee	7.65%	8.65%	9.55%	10.35%	11.05%	11.65%	11.65%	11.65%	11.65%	11.65%	11.65%	11.65%	11.65%	11.65%	11.65%	11.65%
Total	**28.54%**	**31.33%**	**36.73%**	**40.79%**	**43.59%**	**53.02%**	**54.26%**	**54.11%**	**54.24%**	**54.57%**	**54.54%**	**54.58%**	**54.76%**	**54.74%**	**54.66%**	**54.56%**
CORP																
Employer 2/3/	8.57%	9.50%	11.31%	13.68%	14.46%	18.21%	18.71%	18.34%	18.25%	18.28%	18.15%	18.06%	18.07%	17.99%	17.91%	17.84%
Employee	8.40%	8.40%	8.40%	8.40%	8.40%	8.41%	8.41%	8.41%	8.41%	8.41%	8.41%	8.41%	8.41%	8.41%	8.41%	8.41%
Total	**16.97%**	**17.90%**	**19.71%**	**22.08%**	**22.86%**	**26.62%**	**27.12%**	**26.75%**	**26.66%**	**26.69%**	**26.56%**	**26.47%**	**26.48%**	**26.40%**	**26.32%**	**26.25%**
EORP																
Employer	17.42%	17.96%	20.87%	23.50%	23.50%	23.50%	23.50%	23.50%	23.50%	23.50%	23.50%	23.50%	23.50%	23.50%	23.50%	23.50%
Employee	7.00%	11.50%	11.50%	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%	13.00%
Total	**24.42%**	**29.46%**	**32.37%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**	**36.50%**

1/ The ASRS contribution rate for each year includes the contribution rate for long term disability, which is split evenly between the employer and employee.
2/ The employer contribution rate displayed for years FY 2018 through FY 2026 excludes the contribution rate associated with retiree health in PSPRS and CORP. This amount, however, is expected to be minimal in each year (approximately 0.25%).
3/ The employer contribution rate displayed for all years excludes the contribution rate associated with supplemental long term disability insurance (in FY 2017, that rate is 0.27%).