



STATE OF CONNECTICUT

OFFICE OF POLICY AND MANAGEMENT

October 12, 2017

To: Governor Malloy

From: Ben Barnes

Re: Actuarial analysis of 2027 change to exclude overtime from SERS pensions

Following our recent discussions about the legal and practical issues surrounding recent proposals to modify the SERS pension system in 2027, after the current SEBAC agreement expires, I requested an additional analysis from the plan actuary. The purpose of this analysis was to determine the actuarial value of a change to exclude overtime from pensions in 2027 *only for those employees who would not be vested in the pension system at that time.*

As you recall, because all new hires from now on are Tier 4 employees who will vest after 10 years of service, we can surmise that on June 30, 2027 there will be no Tier 4 employees who are yet vested, while virtually all employees of lower tiers will have already vested. As a result, we have concluded that the only way to make a lawful change in 2027 – a change that does not impair the contractual rights of vested employees – would be to limit that change to Tier 4 employees. I am sure you also recall that Tier 4 already contains significant benefit reductions, including reduction in the pensionability of overtime, elimination of the breakpoint, reduction in the pension multiplier, and higher contribution requirements.

Unfortunately, the proposals for 2027 changes that were included in Senate B, the republican budget that you recently vetoed, would have applied changes far more broadly than I believe can be accomplished without impairing the rights of our employees. Indeed, that proposal covered all employees, and – in the case of the COLA change – even retirees who had already retired before the change was put in place. These measures not only would create untenable legal risks for the state, they also drove the calculated actuarial benefit of the changes so that the features of the proposal that were most likely to be determined illegal are the features that accounted for most of the purported “savings.” The attached actuarial analyses on the issue of overtime bear this out.

On September 8, the plan actuaries provided an analysis of the potential reduction in annual state contribution that would occur for the next 30 years if overtime was excluded from final average earnings for all employees who retired after July 1, 2027. That analysis included employees who were already vested prior to 2027. It showed annual contribution savings of \$25 million in the first year growing gradually compared to the current projection of state

pension payments (see Attachment 1.) This analysis made up a significant part of the savings assumed in the republican budget.

On October 11, I received a new valuation of the same overtime proposal, but that excluded those employees who were vested in the pension system before July 1, 2027 – i.e., Tier 4 employees. As you can see on Attachment 2, the first year savings estimate drops dramatically to \$2 million. In that analysis, the savings are shown starting in 2020 because the actuaries assumed the savings from a change in law would be reflected in the next scheduled valuation. The republican budget and the analysis in Attachment 1 assumed that a new valuation would be completed and implemented right away in order to take savings now.

Finally, it is worth noting that both of the attached analyses assume that employee contributions would be calculated only on pensionable earnings. In other words there would be no contribution calculated against overtime earnings in either scenario.

My conclusion from this new analysis is that if the legislature modified the republican proposal to reduce the risk of a successful contract impairment action by limiting the application of changes to unvested employees in 2027, the financial benefit would be dramatically reduced. Furthermore, the very act of requiring an immediate valuation introduces separate contract impairment exposure which could easily cost more than \$2 million to defend. I recommend, therefore, that we continue to strongly oppose any reduction in pension contribution in the FY18-19 budget based on changes to pensions in 2027.

Attachments.

cc: Brian Durand, Chief of Staff
Lisa Egan, Undersecretary
Greg Messner, Assistant Executive Budget Officer

Connecticut SERS
30 Year Projection based on June 30, 2016 Valuation with SEBAC 2017
Assuming 6.90% Investment Return and 2.50% Inflation for All Years in Projection
Overtime Excluded in Final Average Earnings beginning July 1, 2027
(Dollars in Thousands)

Valuation Date 6/30/YYYY (1)	Fiscal Year Ending 6/30/YYYY (2)	Expected Annual Investment Return (3)	Annual Valuation Payoff (4)	Unfunded Liability Beginning of Valuation Year (5)	Funded Assets / Liability (6)	Employer Normal Cost (7)	Amortization of Unfunded Liability (8)	Contributions for Fiscal Year Ending			Total Contribution (12)=(10)+(11)	Besseline Total Svgs
								New Tier Only DC Plan 1% (9)	Total State Contribution (10)=(7)+(9)+(8)	Employee Contribution (11)		
2016	2018	6.90%	3,720,551	20,160,044	37.2%	256,515	1,161,571	0	1,149,086	139,970	1,552,055	1,443,110
2017	2019	6.90%	3,631,506	20,482,983	37.9%	240,626	1,505,725	1,503	1,547,854	134,246	1,882,100	1,574,537
2018	2020	6.90%	3,538,985	20,903,653	38.1%	223,323	1,466,509	2,812	1,692,644	133,925	1,826,569	1,714,913
2019	2021	6.90%	3,451,271	21,337,872	38.1%	191,274	1,639,439	4,289	1,835,002	148,939	1,983,941	1,898,688
2020	2022	6.90%	3,514,625	21,519,045	38.7%	183,622	1,804,400	5,801	1,994,022	154,467	2,148,489	2,019,759
2021	2023	6.90%	3,573,089	21,407,181	40.1%	175,390	1,954,181	7,445	2,137,016	159,553	2,296,569	2,162,477
2022	2024	6.90%	3,620,345	21,136,408	41.3%	164,948	1,971,726	9,118	2,145,792	164,757	2,310,549	2,212,519
2023	2025	6.90%	3,668,639	20,681,543	44.0%	157,439	1,972,444	10,897	2,140,781	170,655	2,311,446	2,168,710
2024	2026	6.90%	3,764,690	20,073,491	46.2%	150,781	1,971,663	12,739	2,135,183	177,317	2,312,500	2,164,221
2025	2027	6.90%	3,840,112	19,478,437	48.3%	143,924	1,970,944	14,711	2,129,579	184,012	2,313,591	2,159,644
2026	2028	6.90%	3,918,740	18,844,585	50.4%	136,289	1,970,355	16,794	2,123,438	190,928	2,314,366	2,154,507
2027	2029	6.90%	3,585,765	18,174,169	52.5%	115,238	1,970,327	18,981	2,104,545	198,154	2,302,699	2,149,737
2028	2030	6.90%	3,665,172	17,409,543	54.7%	109,113	1,966,218	21,262	2,096,593	205,255	2,301,848	2,143,662
2029	2031	6.90%	3,753,448	16,601,684	56.9%	104,319	1,962,570	23,581	2,090,470	212,926	2,303,395	2,138,251
2030	2032	6.90%	3,847,955	15,739,149	59.2%	99,294	1,958,702	25,948	2,083,944	221,147	2,305,091	2,132,828
2031	2033	6.90%	3,949,688	14,815,776	61.6%	94,650	1,480,336	28,342	1,603,328	229,918	1,833,246	1,653,623
2032	2034	6.90%	4,056,623	13,829,974	64.1%	90,071	1,455,901	30,800	1,576,772	238,986	1,815,758	1,628,446
2033	2035	6.90%	4,173,761	13,264,143	65.5%	86,361	1,450,442	33,252	1,570,054	248,775	1,818,829	1,623,248
2034	2036	6.90%	4,298,125	12,679,408	66.9%	83,128	1,446,231	35,733	1,565,091	258,971	1,824,062	1,619,822
2035	2037	6.90%	4,426,283	12,057,188	68.4%	79,630	1,441,905	38,291	1,559,826	269,222	1,829,048	1,615,954
2036	2038	6.90%	4,560,993	11,391,648	70.0%	76,158	1,437,178	40,895	1,554,231	279,769	1,834,000	1,611,665
2037	2039	6.90%	4,701,698	10,679,608	71.7%	72,934	1,432,001	43,542	1,548,477	290,733	1,839,209	1,607,152
2038	2040	6.90%	4,849,587	9,918,656	73.5%	69,908	1,426,401	46,206	1,542,515	302,021	1,844,536	1,602,505
2039	2041	6.90%	5,003,653	9,105,282	75.5%	66,155	1,420,333	48,893	1,538,381	313,586	1,851,967	1,597,575
2040	2042	6.90%	5,163,536	8,237,793	77.7%	62,117	1,413,919	51,623	1,534,660	325,378	1,860,038	1,592,323
2041	2043	6.90%	5,328,897	7,310,043	80.0%	58,270	1,406,926	54,367	1,530,563	337,390	1,867,952	1,587,952
2042	2044	6.90%	5,501,110	6,317,284	82.6%	54,640	1,397,556	57,126	1,514,323	349,718	1,864,041	1,576,690
2043	2045	6.90%	5,680,175	5,257,564	85.4%	50,856	1,350,151	59,902	1,480,228	362,360	1,842,588	1,541,934
2044	2046	6.90%	5,865,861	4,140,318	88.4%	47,056	1,302,937	62,693	1,436,186	375,329	1,811,515	1,497,133
2045	2047	6.90%	6,058,467	2,981,104	91.6%	43,250	1,266,520	65,510	1,403,691	388,639	1,792,330	1,464,020
2046	2048	6.90%	6,258,226	1,787,141	95.0%	39,550	1,066,388	68,454	1,34,966	402,324	1,437,289	1,447,465
				Total		3,667,556	48,059,171	941,510	52,668,237	7,563,381	60,231,618	(1,387,885)

Assumed the rates of retirements will increase in 2026 to reflect the potential behavior of future eligible members.

9/8/2017

Attachment 1

EMM
S.V.N.Y.S

Connecticut SERS
30 Year Projection based on June 30, 2016 Valuation with SEBAC 2017
Assuming 6.90% Investment Return and 2.60% Inflation for All Years in Projection
Overtime Excluded in Final Average Earnings Beginning July 1, 2027 for Only Tier IV who are Not Vested as of July 1, 2027
(Dollars in Thousands)

Valuation Date 6/30/YYYY (1)	Fiscal Year Ending 6/30/YYYY (2)	Expected Annual Investment Return (3)	Annual Valuation Payroll (4)	Unfunded Liability Beginning of Valuation Year (5)	Funded Assets / Liability (6)	Employer Normal Cost (7)	Amortization of Unfunded Liability (8)	Contributions for Fiscal Year Ending			Total Contribution (12)=(10)+(11)	Baseline	Total Svgs
								New Tier Only DC Plan 1% State Match Contribution (9)	Total State Contribution (10)=(7)+(8)+(9)	Employee Contribution (11)			
2016	2018	6.90%	3,720,751	20,359,317	36.9%	262,733	1,180,377	0	1,443,110	133,970	1,577,080	1,443,110	-
2017	2019	6.90%	3,631,506	20,599,835	37.8%	245,705	1,327,329	1,503	1,574,537	134,246	1,708,783	1,574,537	-
2018	2020	6.90%	3,538,985	21,042,571	38.0%	235,089	1,474,858	2,812	1,712,759	133,925	1,846,684	1,712,759	-
2019	2021	6.90%	3,451,271	21,473,165	38.0%	202,818	1,648,403	4,289	1,855,510	148,939	2,004,450	1,855,688	-
2020	2022	6.90%	3,514,625	21,650,910	38.7%	195,646	1,813,918	5,801	2,015,365	154,467	2,169,832	2,015,759	-
2021	2023	6.90%	3,573,089	21,507,345	40.2%	187,518	1,961,868	7,445	2,156,831	159,553	2,316,384	2,162,477	-
2022	2024	6.90%	3,620,345	21,231,478	42.0%	177,378	1,979,045	9,118	2,165,541	164,757	2,330,298	2,172,519	-
2023	2025	6.90%	3,688,639	20,723,073	44.2%	170,120	1,979,527	10,897	2,160,545	170,665	2,331,210	2,164,221	-
2024	2026	6.90%	3,764,690	20,170,608	46.3%	163,688	1,979,287	12,739	2,155,714	177,317	2,333,031	2,159,644	-
2025	2027	6.90%	3,840,112	19,581,132	48.5%	157,004	1,979,120	14,711	2,150,835	184,012	2,334,846	2,154,507	-
2026	2028	6.90%	3,918,740	18,951,844	50.7%	149,577	1,979,012	16,794	2,145,383	190,928	2,336,311	2,149,737	-
2027	2029	6.90%	3,834,662	18,214,705	52.9%	148,073	1,973,416	18,981	2,140,471	198,154	2,338,625	2,143,662	-
2028	2030	6.90%	3,884,880	17,500,137	55.1%	139,000	1,973,589	21,262	2,133,851	205,255	2,339,106	2,138,251	-
2029	2031	6.90%	3,965,534	16,700,650	57.4%	131,589	1,970,748	23,581	2,125,919	212,926	2,338,844	2,132,828	-
2030	2032	6.90%	4,043,653	15,843,306	59.7%	124,102	1,967,437	25,948	2,117,487	221,147	2,338,634	2,126,918	-
2031	2033	6.90%	4,130,129	14,924,539	62.1%	117,243	1,489,594	28,342	1,635,179	229,918	1,865,097	1,619,822	-
2032	2034	6.90%	4,222,300	13,943,280	64.6%	110,495	1,465,686	30,800	1,606,991	238,986	1,845,977	1,628,446	-
2033	2035	6.90%	4,326,443	13,981,160	66.0%	105,005	1,460,719	33,252	1,598,976	248,775	1,847,751	1,623,248	-
2034	2036	6.90%	4,438,735	12,799,851	67.4%	100,172	1,456,987	35,733	1,592,892	258,971	1,851,862	1,615,954	-
2035	2037	6.90%	4,554,987	12,180,965	68.9%	95,046	1,453,152	38,291	1,586,490	269,222	1,855,712	1,611,665	-
2036	2038	6.90%	4,677,492	11,518,204	70.4%	90,013	1,448,892	40,895	1,579,800	279,769	1,859,569	1,607,152	-
2037	2039	6.90%	4,807,912	10,808,340	72.1%	85,333	1,444,133	43,542	1,573,029	290,733	1,863,761	1,602,505	-
2038	2040	6.90%	4,945,678	10,048,955	73.9%	80,956	1,438,965	46,206	1,566,127	302,021	1,868,149	1,597,575	-
2039	2041	6.90%	5,090,245	9,236,558	75.9%	76,936	1,433,284	48,893	1,559,114	313,586	1,872,700	1,586,761	-
2040	2042	6.90%	5,240,972	8,369,515	78.0%	75,272	1,427,239	51,623	1,549,816	325,378	1,879,513	1,576,690	-
2041	2043	6.90%	5,397,725	7,443,558	80.3%	74,691	1,420,725	54,367	1,540,904	337,390	1,887,205	1,566,878	-
2042	2044	6.90%	5,562,056	6,452,366	82.8%	74,396	1,409,382	57,126	1,530,517	349,718	1,890,622	1,549,934	-
2043	2045	6.90%	5,733,930	5,393,912	85.5%	74,323	1,370,292	59,902	1,504,517	362,360	1,866,878	1,497,133	-
2044	2046	6.90%	5,913,047	4,267,180	88.5%	74,452	1,323,581	62,693	1,460,726	375,329	1,836,055	1,464,020	-
2045	2047	6.90%	6,099,610	3,099,877	91.6%	74,757	1,288,104	65,510	1,428,370	388,639	1,817,009	1,447,622	-
2046	2048	6.90%	6,293,867	1,895,830	94.8%	75,194	(98,350)	68,454	1,428,370	402,324	1,817,009	1,447,622	-
				Total			4,074,325	48,420,366	941,510	53,436,221	7,563,381	60,999,601	(619,902)

Assumed the rates of retirements will increase in 2026 to reflect the potential behavior of future eligible members.

10/11/2017

Attachment 2

Annex 1
Savvas