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Frequently Asked Questions on Employer Rates for Fiscal Years 2020 and 2021

Here are answers to some common questions regarding the recently certified New Hampshire Retirement System (NHRS, the retirement system) employer contribution rates for fiscal years 2020 and 2021.

The 2020-21 rates for the State of New Hampshire and for political subdivision employers, which were certified by the NHRS Board of Trustees on September 11, 2018, are available on the NHRS website at: https://www.nhrs.org/employers/employer-contribution-rates

1. Why are the rates changing?

Employer contribution rates are set every two years pursuant to RSA 100-A:16, III. The rates are developed as part of a biennial actuarial valuation, which is required by statute to determine the actuarially sound rates necessary to maintain the retirement system trust fund at the level needed to meet its future obligations.

The contribution rates for fiscal years 2020 and 2021 are based on the actuarial valuation as of June 30, 2017. In the aggregate, employer contributions are decreasing slightly from 2018-19. Rates declined for the Employee, Police and Fire groups, and increased slightly for Teachers. (See questions 2 and 3 for additional information on the Teacher rate.)

2. How are the rates determined?

GRS, the retirement system's consulting actuary, calculates the cost of future benefits, the unfunded actuarial accrued liability (UAAL), and employer contribution rates based on assumptions about many future events, such as the age when members will retire, their rate of salary growth, how long they will live after retirement, and how much the plan's investments will earn.

Employer contribution rates for three of the four membership classifications – Group I Employees, Group II Police and Group II Fire – have decreased between 0.21 percent to 1.8 percent of covered payroll compared to the current rates, primarily due to strong investment performance over the five-year period ending June 30, 2017.

Despite the investment gains, employer contribution rates for Group I Teachers will increase by 0.44 percent of covered payroll due to a reduction to the actuarial assumption for teacher payroll growth adopted by the Board in April in response to the continuing decline in the number of active teachers.

3. Why did the Board adjust the payroll growth assumption for the Teacher group?

This was a decision driven by the demographic experience of teachers. When the Board adopted improved actuarial assumptions in May 2016, the teacher payroll growth assumption was set at 3.0 percent, lower than the 3.25 percent assumption for all other member groups (Employee, Police, and Fire) to compensate for an anticipated 0.25 percent annual decrease in the number of active teachers due to the ongoing decline in New Hampshire's school-age population. However, the number of active NHRS Teacher members has decreased nearly 5 percent since 2008 and payroll growth has continued to lag expectations. The most recent state population projections from the New Hampshire Office of Strategic Initiatives show a declining school age population through 2025. As a result, the Board voted in April to reduce the payroll growth assumption for teachers by an additional .25 percent to 2.75 percent.

4. Does the NHRS Board of Trustees have any leeway when certifying employer rates?

No. There is no discretion in setting employer rates. State law requires that the NHRS Board of Trustees certify actuarially sound rates necessary to keep the retirement system on track to meet its long-term obligations; the New Hampshire Constitution (Part I, Article 36-a) requires employers to pay those rates in full.

The relevant section of Article 36-a reads, in part:

"The employer contributions certified as payable to the New Hampshire retirement system … as shall be determined by sound actuarial valuation and practice … shall be appropriated each fiscal year to the same extent as is certified."

In addition to the constitutional mandate, Trustees are also bound by their fiduciary duty to the pension plan, which is the highest standard of conduct under the law. When NHRS fiduciaries make decisions about benefit administration, investments, or any other subject that falls within their statutory responsibilities, they are required to act solely in the best interest of the collective membership, not on behalf of individual members or member groups, employers, lawmakers, taxpayers, or anyone else who might have an interest in the outcome of the decision.

5. Why are there different rates for each of the member classifications?

Employer contribution rates for Employee, Teacher, Police, and Fire members are determined separately based on benefit structure, demographics, and other information unique to each member classification, so rates vary among the different classifications. Group II rates are higher because the retirement age for Police and Fire members is lower and the Group II benefit formula produces a larger pension than the Group I benefit formula. (Note: Group II members are not eligible for Social Security benefits for their NHRS-covered employment; neither they nor their employers pay Social Security taxes.)

In addition to the pension costs, the employer rates also contain a Medical Subsidy rate (see Question 7) that ranges from 0.29 percent to 3.66 percent of covered payroll, depending on the member classification.

6. How does the unfunded pension liability affect employer contribution rates?

There are three components to employer contribution rates: the normal cost, the unfunded liability, and the Medical Subsidy.

The normal cost reflects the estimated actuarial cost of pension benefits as those benefits are earned each year by members. This cost is shared by the employer and the member, with members paying the majority of the normal cost. The normal cost will decline over time due to 2011 legislative changes that reduced benefit provisions for new members hired on or after July 1, 2011, as well as any member hired prior to that date but not vested prior to January 1, 2012.

The unfunded actuarial accrued liability (UAAL) is the estimated value of NHRS benefits that have been earned in the past, but have not yet been funded. The current unfunded liability, which is being amortized through 2039, is borne solely by the employers. Overall, the unfunded liability accounts for more than 70 percent of the total employer contribution rate.

There have been several contributing factors to the current NHRS unfunded liability:

- A flawed statutory funding methodology in effect from 1991-2007 that led to the long-term under-calculation of employer contributions;
- The diversion of approximately $900 million in investment earnings from the pension trust into a "Special Account" over roughly the same period. (The Special Account, which was created by legislation in the 1980s and repealed in 2012, funded other post-retirement benefits such as cost-of-living adjustments);
- Global economic dips (the 2001-02 dot com bubble and the great financial crisis of 2008-09) negatively impacting investment performance;
- Adoption of more conservative actuarial assumptions in 2011 and 2016 by the NHRS Board of Trustees, based on the results of five-year actuarial experience studies required by statute and the Board's Actuarial Funding Policy. Changes to the assumptions for investment returns, payroll growth and mortality increased the UAAL and financially strengthened the retirement system trust fund by generating additional revenue through increases to employer contribution rates.

Despite the unfunded liability, retirement benefits for NHRS members are secure. Changes made in recent years have put NHRS on a solid path to financial health, however, the unfunded liability took many years to create, and it will take many years to eliminate it.

In 2018, legislation was enacted to recognize actuarial gains and losses incurred in future bienniums over closed periods of no more than 20 years. This is referred to as "layered amortization." This approach will separately track the sources of changes to the UAAL (i.e. benefit revisions, investment gains/losses, or changes to assumptions), spread future actuarial gains and losses more evenly over time, avoid some of the potential employer contribution rate volatility as 2039 approaches, and provide a plan to deal with gains and losses incurred beyond 2039. This change does not impact the amortization of the retirement system's existing UAAL – $5.04 billion at 6/30/17 – which will continue to be fully funded through FY 2039.

7. Why is the Medical Subsidy included in the employer rate?

The Medical Subsidy is a payment made by NHRS directly to an eligible retiree's former employer or the employer's health insurance administrator that goes toward the cost of health insurance for a qualified retired member, spouse, or dependent child(ren). The Medical Subsidy is not a health insurance plan.

Medical Subsidy benefits are funded from a 401(h) trust for political subdivision Employees, state Employees, Teachers, and Police and Fire members. Because these benefits are pay-as-you-go, employers are required by statute to pay the minimum rate necessary to maintain the benefits provided for each of the above groups under RSA 100-A:53, RSA 100-A:53-b, RSA 100-A:53-c and RSA 100-A:53-d.

Because this benefit is a closed plan except with respect to certain Group II members, the Medical Subsidy rates are expected to decrease in future years.

8. Does the State of New Hampshire pay any portion of the political subdivision employer rates?

No. In 2012, the New Hampshire Supreme Court upheld statutory changes to RSA 100-A:16 enacted in 2009 that reduced the percentage the State of New Hampshire paid toward employer retirement contributions for Teacher, Police, and Fire members employed by political subdivisions. Those contributions were subsequently eliminated entirely with the enactment of House Bill 2 in 2011.

The Supreme Court decision did not change the total amount of employer contributions that must be paid to the retirement system – it only upheld the State's authority to reduce, and eventually eliminate, its contribution toward employer retirement contributions for Teacher, Police, and Fire members employed by political subdivisions. The net result of the decision was to shift pension costs from the State to political subdivisions.

When RSA 100-A:16 was enacted in 1967, the State was responsible for 40 percent of the employer contribution for Teacher members employed by political subdivisions. The statute was amended in 1977, requiring the State to pay 35 percent of the employer contributions for Teacher, Police, and Fire members employed by political subdivisions.

RSA 100-A:16 was amended in 2009 to reduce the State's share to 30 percent in Fiscal Year 2010 and 25 percent in Fiscal Year 2011. The 2009 amendment also restored the State contribution to 35 percent in Fiscal Year 2012. However, the statute was amended again in 2011 to eliminate the State's percentage share of employer contributions altogether. The 2011 amendment also included a one-time transitional appropriation of $3.5 million in an effort to offset political subdivision employer contributions in Fiscal Year 2012.

9. What are the member contribution rates?

Member contribution rates are set by statute. Group I (Employee, Teacher) members contribute 7 percent of their Earnable Compensation to the retirement system. Group II (Police, Fire) members contribute 11.55 percent and 11.80 percent, respectively. Note: Police and Fire members are not eligible for Social Security.

10. Have the updated financial reporting standards promulgated in recent years by the Governmental Accounting Standards Board (GASB) impacted employer contribution rates?

No. There is a statutory funding mechanism to pay down the NHRS UAAL, which is not affected by GASB's changes to financial accounting reporting requirements for participating state and local governments. (Note: GASB 68 and GASB 75 reporting requirements also have no impact on local property tax rates.)

For reference, GASB Statement 68 requires each participating employer to report its proportionate share of the retirement system's net pension liability (NPL) on its balance sheet. Previously, employers were only required to report the annual contributions they made to the retirement system. GASB Statement 75 adds a similar requirement regarding any other post-employment benefits (OPEB) provided by an employer to its retirees.

For more information on GASB, see: www.nhrs.org/employers/gasb

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Related links:
NHRS … Now You Know: Demystifying 'unfunded liability':
https://www.nhrs.org/docs/default-source/now-you-know/now_you_know_uaal.pdf
NHRS … Now You Know: Fiduciary: A word worth knowing:
https://www.nhrs.org/docs/default-source/now-you-know/now_you_know_10_fiduciary.pdf
NHRS Employer and Member Rates since 1971:
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RSA 100-A:
www.gencourt.state.nh.us/rsa/html/vi/100-a/100-a-mrg.htm
NH Constitution Article 36-a:
www.nhrs.org/about-nhrs/laws-administrative-rules