The ADVISOR
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AEA Lawsuit Could Ruin the Education Budget

EDITORIAL

If AEA is successful in the lawsuit it filed against PEEHIP, there could be dire consequences for the education budget, which in turn would hurt active and retired education employees. TRS members should be aware that if AEA prevails in the Alabama Supreme Court and the PEEHIP premium increases that were effective October 1, 2016, are permanently invalidated and repaid to members, it will create a **$172 million deficit** in the PEEHIP budget through the next fiscal year (FY 2019).

The deadline for making PEEHIP's FY 2019 budget request to the Legislature has already passed. PEEHIP requested $800 per employee per month to fund PEEHIP. PEEHIP also informed the Executive Budget Office that if PEEHIP loses the AEA lawsuit, the budget request would have to be raised to make up for the $172 million shortfall. In that event, the request

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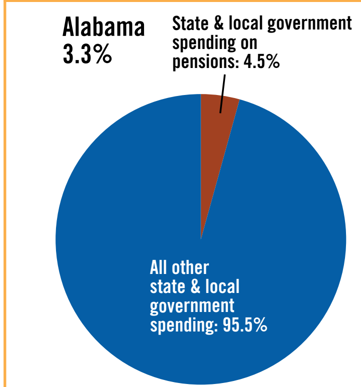
Figure 1. State and local spending on public pensions as a percentage of total government direct general spending. FY 14



Compiled by NASRA based on U.S. Census Bureau data

The 2016 ERS Actuary Results

BY CAVANAUGH MACDONALD

Note: Employer (taxpayer) costs only 0.41% for state employees and 3.62% for state police for Tier II. State employees are paying 93.6% and state police are paying 73.4% of their benefit for Tier II.

	STATE EMPLOYEES	STATE POLICEMEN	LOCAL EMPLOYEES (875 Local Units)
VALUATION DATE	**September 30, 2016**	**September 30, 2016**	**September 30, 2016**
Number of active members	29,101	655	55,058
Annual compensation	$ 1,265,310,969	$ 41,213,571	$ 2,266,366,656
Number of retired members and beneficiaries*	23,614	893	23,242
Annual retirement allowances*	$ 513,858,040	$ 41,425,353	$ 450,027,767
Number of deferred vested members	942	13	1,155
Estimated deferred annual allowances	$ 11,332,390	$ 214,321	$ 13,193,635
Assets:			
Actuarial value	$ 4,598,818,390	$ 318,102,553	$ 6,165,358,692
Market value	$ 4,615,916,406	$ 318,884,908	$ 6,173,636,004
Unfunded actuarial accrued liability	$ 2,805,769,277	$ 272,554,851	$ 2,567,404,790
Funded Ratio based on Actuarial Value of Assets	62.1%	53.9%	70.6%
CONTRIBUTIONS FOR FISCAL YEAR ENDING	**September 30, 2019**	**September 30, 2019**	**September 30, 2019**
Tier I (first hired prior to January 1, 2013)			
Employer contribution rate			
Normal	0.78%	10.27%	Varies
Accrued liability	13.36	39.44	Varies
Death benefit	0.02	0.02	0.02%
Administration	0.35	0.35	0.35
Total	14.51%	50.08%	Varies
TIER II (first hired on or after January 1, 2013)			
Employer contribution rate			
Normal	0.41%	3.62%	Varies
Accrued liability	13.36	39.44	Varies
Death benefit	0.02	0.02	0.02%
Administration	0.35	0.35	0.35
Total	14.14%	43.43%	Varies
Blended Amortization period	29.3 years	29.3 years	Varies

*Includes post-DROP members in suspended status who are also active with a second retirement account.

Cost of Employer Health Plans Rising

AND THE SHARE OF FIRMS THAT OFFER COVERAGE CONTINUED TO DECLINE IN 2017, ACCORDING TO A SURVEY

BY ANNA WILDE MATHEWS, *THE WALL STREET JOURNAL*

The average cost of health coverage offered by employers pushed toward $19,000 for a family plan this year, while the share of firms providing insurance to workers continued to edge lower, according to a major survey.

Annual premiums rose 3% to $18,764 for an employer plan in 2017, from $18,142 last year, the same rate of increase as in 2016, according to an annual poll of employers performed by the nonprofit Kaiser Family Foundation along with the Health Research & Educational Trust, a nonprofit affiliated with the American Hospital Association.

The trend of relatively gradual premium increases has continued for several years, with the growth of premiums damped by a shift toward bigger out-of-pocket costs for employees in the form of high deductibles—a move that slowed this year, as average deductibles were roughly flat compared with 2016.

Still, the rise of premiums over time has resulted in family health plans that can annually cost more than a new car, with the cost split between firms and employees. Employees paid on average $5,714, or 31%, of the premiums, for a family plan in 2017, according to Kaiser.

For an individual worker, the average annual cost of employer coverage was $6,690 in the 2017 survey, or 4% higher than last year, with employees paying 18% of the total.

Another trend was also sustained in the 2017 survey: a decline in the share of employers offering health insurance despite a labor market that shows signs of tightening—at least in certain regions and sectors. The move has been driven by a drop-off among the smallest firms.

This year, 53% of employers in the survey offered health benefits, down from 56% last year and 61% in 2012. Just half of firms with 3 to 49 workers offered health insurance this year, the first time the share reached that threshold. Five years ago, 59% of companies in that category offered health benefits.

Gary Claxton, a vice president at the foundation, said that the overall cost of insurance appears to be driving small firms, particularly those with low-wage workers, to stop offering health benefits. Indeed, among small employers that didn't offer health insurance, 44% said the biggest reason for not providing the benefit was its cost. "It's harder for them to maintain coverage when it's so expensive," Mr. Claxton said.

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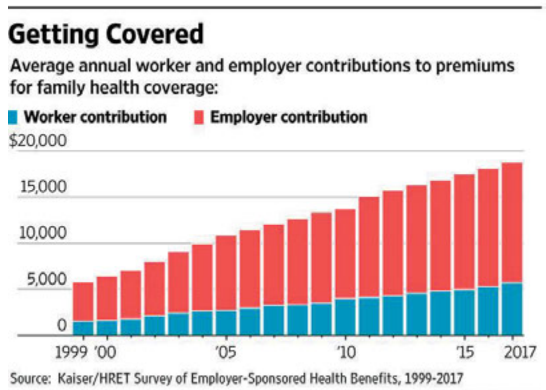
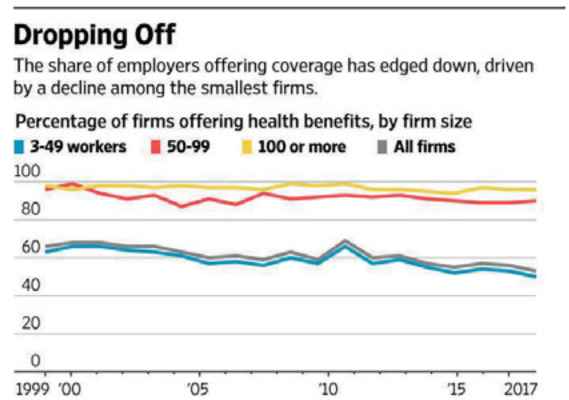


Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2017
THE WALL STREET JOURNAL.



Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2017
THE WALL STREET JOURNAL.

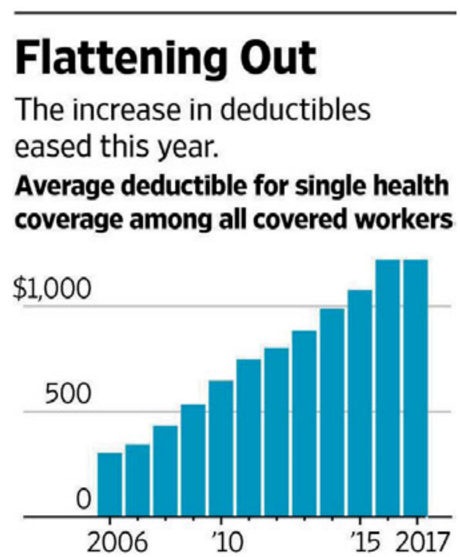
AEA Lawsuit CONTINUED FROM PAGE ONE

would be increased to $956 per employee per month – which would be **$1,872 more per year for every eligible education employee**.

It is unlikely the growth in the Education Trust Fund (ETF) would be enough to make up that shortfall. To put the shortfall in perspective, for FY 2018 there was only $90 million of additional money in the ETF for **all** increased costs for education programs (including K4, equipment, transportation, buildings, etc.) and employees (including increased healthcare costs).

Last year, the Legislative Fiscal Office estimated that each 1% raise in salary for all education employees would cost about $41 million. Even if there is $172 million more in revenue in FY 2019 to make up the shortfall AEA's lawsuit could create, after funding that deficit there would be no money left for any increased education expenses, **including pay raises for education employees**. This is because the amount required to pay increased healthcare costs comes straight from the same budget that funds education employee salaries.

PEEHIP doesn't like increased premiums any more than the members do, but the reality is that healthcare costs continue to rise. As a consequence, the only choices available to pay for those increases are either to cut benefits or have the members and the Legislature contribute more money.



Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2017
THE WALL STREET JOURNAL.

Five Retirement Expenses Most People Underestimate

BY MAURIE BACKMAN, TMFBOOKNERD

When we think about retirement, many of us are wired to assume that our costs will naturally drop as a result of no longer working. But we may be overestimating the extent to which that might happen. While it's true that some expenses, like commuting, go down in retirement, others are, in fact, likely to climb. Here are five in particular that tend to catch retirees off guard.

1. HEALTHCARE

Healthcare is probably the one expense with a higher tendency to go up rather than down in retirement. That's partly because Medicare has its limitations, and countless seniors are forced to pay for a wide range of services that may have been covered during their working years. According to recent projections, the average healthy 65-year-old couple today will spend a whopping $400,000 or more on medical costs in retirement. Reading between the lines, if you're not particularly healthy, you can, and should, expect to see that number climb even higher.

2. HOUSING

Though housing doesn't always go up for retirees, it can be a pricier prospect than anticipated. Even if you're among the 70% of seniors who manage to pay off their mortgages in time for retirement, you can't forget about the peripheral costs of homeownership, such as property taxes and maintenance. In fact, property taxes actually have a tendency to rise over time, even during periods where the housing market itself underperforms. Furthermore, it costs the average homeowner 1% to 4% of his or her home's value to keep up with maintenance each year. Since retirees tend to own older properties, you may inevitably wind up hitting the highest end of that range, which could throw your budget off-track.

3. ENTERTAINMENT

When you're not spending 40 hours or more at the office each week, it stands to reason that you'll need to get creative and find ways to fill that newfound free time. And while you don't necessarily have to spend a bundle on travel and leisure, you should by no means count on your entertainment costs going down once you stop working. In fact, you'd be surprised at how a few discounted museum entries and movie tickets a week can really add up over the course of a given year. It's estimated that 58% of workers fail to account for leisure spending in retirement, so rather than discount the amount you'll spend, factor it into your budget.

4. TAXES

Contrary to what many retirees are led to believe, taxes can constitute a significant financial burden during retirement. Not only will you pay taxes on withdrawals from a traditional 401(k) or IRA – withdrawals that you're actually required to start taking upon reaching age 70 1/2 – but you'll also pay taxes on traditional investment income, interest on money in the bank, and, in some cases, a large chunk of your Social Security benefits.

Now the good news is that you do have some options for lowering your taxes down the line, whether it's moving your savings from a traditional retirement plan to a Roth account, or shifting some investments into municipal bonds, which always offer federal tax-exempt interest payments. But if you don't adopt some sort of tax-saving strategy, you may come to find that you're losing a huge portion of your retirement income to taxes alone.

5. LONG-TERM CARE

While you may not necessarily picture yourself living out your senior years in a nursing home or specialized facility, a staggering 70% of seniors wind up needing some type of long-term care. And if you don't save enough to cover those costs, or get yourself a comprehensive insurance plan, you may be in for a shock during retirement.

According to recent projections, it costs over $82,000 a year to reside in a nursing home, and that's for a shared room – a private one will set you back upward of $90,000 annually. Furthermore, the average assisted living facility charges more than $43,000 per year. If you don't read up on these costs and come up with a game plan for covering them should they arise, you may be in for a world of financial shock at a time.

Underestimating your senior living costs could be one of the greatest retirement mistakes you'll ever make. Rather than take your chances, read up on how seniors today are spending their money, and see how well your savings are likely to stack up. You may need to adjust your current retirement plan to ensure that you don't run short on money later in life.

Other States and Taxes

SOURCE: *BLOOMBERG* AND *THE NEW YORK TIMES*

In its June 2017 state revenue report, the Rockefeller Institute of Government has this to say: "States have been forecasting weak revenue growth for fiscal 2017, with only 3.6 percent growth in the income tax and 3.1 percent growth in the sales tax. Several states had already reduced their revenue forecasts for fiscal 2017 in the post-election period. Despite the downward revisions, state revenue forecasts for fiscal year 2017 are likely to be reduced further. We anticipate actual tax revenue collections will be short of the forecasts in the typical state once states close the budget books for fiscal year 2017."

Albert Hunt wrote a column for *Bloomberg* entitled "Americans Aren't So Excited About Tax Reform." He cites a *Bloomberg* poll conducted July 8-12 showing that only 4% of Americans see taxes as the most important issues facing the country. "By contrast, 35% said they considered healthcare to be the No. 1 issue. Concerns about jobs, terrorism, and climate change also ranked far ahead of taxes."

Supply-side economics was born in 1977 – 40 years ago. We were present at the revolution and have long believed that lower tax rates spur economic growth. But times change. A *The New York Times* article entitled "Cut Taxes? In states, G.O.P. Goes Other Way," presents how the tide might be running out on tax-cutting fever.

Conservative lawmakers in Kansas, South Carolina, and Tennessee have agreed to significant tax increases in recent weeks to meet demands for more revenue. They are challenging what has become an almost dogmatic belief for their party, and sharply diverging from President Trump as he pushes for what his administration has billed as the largest tax cut in at least a generation.

And now some Republicans say that what has played out in these states should serve as a cautionary tale in Washington, where their party's leaders are confronting a set of circumstances that looks strikingly similar.

The debate promises to test the enduring relevance of one of the most fundamental principles of modern conservatism – supply side economics, the idea that if you cut taxes far enough, the economy will expand to the point that it generates new tax revenue.

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Cost of Employee Heath Plans Rising

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However, among small employers that didn't provide health coverage, 16% did give workers some money they could use toward purchasing a plan themselves.

Kaiser foundation officials said it wasn't clear why the growth in deductibles appeared to pause this year. The average general deductible for single coverage among all workers, including those with no deductible, this year was $1,221. That is the same as last year, but up sharply from $802 in 2012. This year, 28% of covered workers were enrolled in high-deductible plans that can be paired with savings accounts that aren't taxed, compared with 29% last year and 19% five years ago.

Drew Altman, chief executive of the Kaiser foundation, said it was too soon to tell if the growth in deductibles would quickly resume next year, or if employers are reluctant to keep pushing the tactic.

"We'll have to watch it," Mr. Altman said. "It's possible it's playing itself out or reaching some kind of natural limit."

One factor that had helped encourage the adoption of higher-deductible plans, a tax in the Affordable Care Act on high-cost employer coverage, is now slated to take effect in 2020. But it has drawn opposition from both Democrats and Republicans. Employers may be assuming that it is unlikely the tax will ever hit, easing the urgency on ratcheting up deductibles.

The Kaiser survey was conducted between January and June of this year and included 2,137 randomly selected employers that responded to the full telephone survey.

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The Retirement Systems of Alabama
201 South Union Street
P.O. Box 302150
Montgomery, Alabama 36130-2150
Phone: 334.517.7000
877.517.0020
RSA Website: www.rsa-al.gov