EXHIBIT "Z"
APPROPRIATIONS HANDBOOK

STATE OF NEW JERSEY

FISCAL YEAR

2014 - 2015

DEPARTMENT OF THE TREASURY

OFFICE OF MANAGEMENT AND BUDGET

Andrew P. Sidamon-Eristoff
State Treasurer

Charlene M. Holzbaur
Director, Office of Management and Budget
NEW JERSEY STATE LEGISLATURE
BUDGET AND APPROPRIATIONS COMMITTEES
SESSION OF 2014

SENATE BUDGET AND APPROPRIATIONS COMMITTEE

Paul A. Sarlo (D), 36th District (Parts of Bergen and Passaic), Chairman
Brian P. Stack (D), 33rd District (Part of Hudson), Vice-Chairman
Peter F. Barnes III (D), 18th District (Part of Middlesex)
Jennifer Beck (R), 11th District (Part of Monmouth)
Anthony R. Bucco (R), 25th District (Parts of Morris and Somerset)
Sandra B. Cunningham (D), 31st District (Part of Hudson)
Linda R. Greenstein (D), 14th District (Parts of Mercer and Middlesex)
Kevin J. O'Toole (R), 40th District (Parts of Bergen, Essex, Morris and Passaic)
Steven V. Oroho (R), 24th District (Sussex and parts of Morris and Warren)
Nellie Pou (D), 35th District (Parts of Bergen and Passaic)
M. Teresa Ruiz (D), 29th District (Part of Essex)
Samuel D. Thompson (R), 12th District (Parts of Burlington, Middlesex, Monmouth and Ocean)
Jeff Van Drew (D), 1st District (Cape May and parts of Atlantic and Cumberland)

GENERAL ASSEMBLY BUDGET COMMITTEE

Gary S. Schaer (D), 36th District (Parts of Bergen and Passaic), Chairman
John J. Burzichelli (D), 3rd District (Salem and parts of Cumberland and Gloucester) Vice-Chairman
Christopher J. Brown (R), 8th District (Parts of Atlantic, Burlington, and Camden)
Anthony M. Bucco (R), 25th District (Parts of Morris and Somerset)
Joseph Cryan (D), 20th District (Part of Union)
Gordon M. Johnson (D), 37th District (Part of Bergen)
Eliana Pinnor Marin (D), 29th District (Part of Essex)
Raj Mukherji (D), 33rd District (Part of Hudson)
Dreilan J. O'Scanlon (R), 13th District (Part of Monmouth)
Troy Singleton (D), 7th District (Part of Burlington)
Joy Weber (R), 26th District (Parts of Essex, Morris and Passaic)
Benjie E. Wimberly (D), 35th District (Parts of Bergen and Passaic)

David J. Rosen, Legislative Budget and Finance Officer, Office of Legislative Services
Frank W. Haines III, Assistant Legislative Budget and Finance Officer, Office of Legislative Services
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Pad63
TO ALL DEPARTMENTS AND AGENCIES

Attention is directed to section one of the Appropriations Act (P.L. 2014, c.14) with reference to the availability of the appropriations for the period of one month after the close of said period fiscal year. State officers are advised that, by reason of the enactment of this clause, all unexpended balances will lapse, unless otherwise provided, at the close of the one-month period unless they are reserved as provided therein.

Transmittals of funds deposited by each State agency shall be forwarded to the Division of Budget and Accounting in accordance with existing regulations. Each State agencies' deposits will be credited to the appropriate account. Receipts which may be appropriated to any State agency may be expended only in accordance with the provisions of the Act.

State agencies shall forward bills for payment as soon as practicable. Every effort will be made by the Department of the Treasury to facilitate payment, particularly those bills subject to discount.

Note: This publication incorporates additional language provisions from P.L. 2014, c.15, which amended and supplemented the Appropriations Act.
**GOVERNOR'S REVENUE CERTIFICATION**

**ANTICIPATED RESOURCES FOR**

**THE FISCAL YEAR 2014-2015**

**GENERAL FUND**

(Thousands of dollars)

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Undesignated Fund Balance, July 1, 2014</td>
<td>$3,000,000</td>
</tr>
<tr>
<td><strong>Total Undesignated Fund Balance</strong></td>
<td><strong>100,000</strong></td>
</tr>
</tbody>
</table>

**Major Taxes**

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>$9,313,000</td>
</tr>
<tr>
<td>Motor Vehicle Fees</td>
<td>$432,400</td>
</tr>
<tr>
<td>Motor Fuel</td>
<td>$215,000</td>
</tr>
<tr>
<td>Mental Health Insurance</td>
<td>$21,700</td>
</tr>
<tr>
<td>Public Utility Excise (Refund)</td>
<td>$14,000</td>
</tr>
<tr>
<td>Corporation Banks and Financial Institutions</td>
<td>$210,000</td>
</tr>
<tr>
<td>Cigarettes</td>
<td>$180,751</td>
</tr>
<tr>
<td>Alcoholic Beverage Excise</td>
<td>$110,000</td>
</tr>
<tr>
<td>Tobacco Products Wholesale Sales</td>
<td>$110,000</td>
</tr>
<tr>
<td>Premium Products Gross Receipts</td>
<td>$305,000</td>
</tr>
<tr>
<td>Insurance Premium</td>
<td>$627,000</td>
</tr>
<tr>
<td>Transfer and Inheritance</td>
<td>$757,900</td>
</tr>
<tr>
<td>Corporation Business</td>
<td>$2,610,000</td>
</tr>
<tr>
<td>Sales Tax Dedication</td>
<td>$(693,000)</td>
</tr>
<tr>
<td><strong>Total Major Taxes</strong></td>
<td><strong>14,644,751</strong></td>
</tr>
</tbody>
</table>
### 3. EDUCATIONAL, CULTURAL, AND INTELLECTUAL DEVELOPMENT

#### 34. EDUCATIONAL SUPPORT SERVICES

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPP Account No.</th>
<th>Description</th>
<th>Amount (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-150-034-5089-001</td>
<td>5089-100-300000-12</td>
<td>Salary and Wages</td>
<td>1,283</td>
</tr>
<tr>
<td>15-150-034-5089-002</td>
<td>5089-100-300000-2</td>
<td>Materials and Supplies</td>
<td>30</td>
</tr>
<tr>
<td>15-150-034-5089-003</td>
<td>5089-100-300000-3</td>
<td>Services Other Than Personal</td>
<td>341</td>
</tr>
<tr>
<td><strong>Total Appropriation, Early Childhood Education</strong></td>
<td></td>
<td></td>
<td><strong>1,654</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPP Account No.</th>
<th>Description</th>
<th>Amount (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-150-034-5089-004</td>
<td>5089-100-310000-12</td>
<td>Salary and Wages</td>
<td>4,712</td>
</tr>
<tr>
<td>15-150-034-5089-005</td>
<td>5089-100-310000-2</td>
<td>Materials and Supplies</td>
<td>36</td>
</tr>
<tr>
<td>15-150-034-5089-006</td>
<td>5089-100-310000-3</td>
<td>Services Other Than Personal</td>
<td>385</td>
</tr>
<tr>
<td>15-150-034-5089-008</td>
<td>5089-100-310000-4</td>
<td>Maintenance and Fixed Charges</td>
<td>7</td>
</tr>
<tr>
<td><strong>Total Appropriation, School Improvement</strong></td>
<td></td>
<td></td>
<td><strong>5,140</strong></td>
</tr>
<tr>
<td><strong>Total Appropriation, School District Improvement</strong></td>
<td></td>
<td></td>
<td><strong>6,794</strong></td>
</tr>
</tbody>
</table>

#### 39. TEACHERS' PENSION AND ANNUITY ASSISTANCE

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPP Account No.</th>
<th>Description</th>
<th>Amount (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-150-034-5089-009</td>
<td>5089-100-320000-00</td>
<td>Teachers' Pension and Annuity Fund - Post Retirement Medical (PERS)</td>
<td>852,999</td>
</tr>
<tr>
<td><strong>Total Appropriation, Teachers' Pension and Annuity Assistance</strong></td>
<td></td>
<td></td>
<td><strong>2,411,753</strong></td>
</tr>
</tbody>
</table>

**40. EDUCATIONAL SUPPORT SERVICES - General Fund**

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPP Account No.</th>
<th>Description</th>
<th>Amount (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-150-034-5089-010</td>
<td>5089-100-320000-01</td>
<td>Teachers' Pension and Annuity Fund</td>
<td>2,103,283</td>
</tr>
<tr>
<td>15-150-034-5089-011</td>
<td>5089-100-320000-02</td>
<td>Teachers' Pension and Annuity Fund (PERS)</td>
<td>361,520</td>
</tr>
<tr>
<td>15-150-034-5089-012</td>
<td>5089-100-320000-03</td>
<td>Teachers' Pension and Annuity Fund - Non-contributory Insurance (PERS)</td>
<td>2,411,753</td>
</tr>
</tbody>
</table>

**Language -- Direct State Services - General Fund**

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPP Account No.</th>
<th>Description</th>
<th>Amount (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-150-034-5089-013</td>
<td>5089-100-320000-04</td>
<td>Teachers' Pension and Annuity Fund - Post Retirement Medical (PERS)</td>
<td>2,411,753</td>
</tr>
</tbody>
</table>

**Language -- Grants-In-Aid - General Fund**

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPP Account No.</th>
<th>Description</th>
<th>Amount (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-150-034-5089-014</td>
<td>5089-100-320000-05</td>
<td>Teachers' Pension and Annuity Fund</td>
<td>2,411,753</td>
</tr>
</tbody>
</table>

**Receipts from the State Board of Examiners' fees in excess of those anticipated, not to exceed $1,200,000, and the unexpended program balances at the end of the preceding fiscal year, are appropriated for the operation of the Professional Development and Licensing programs.**

The amount hereinabove appropriated for the Liberty Science Center - Educational Services shall be used to provide educational services to districts with high concentrations of at-risk students in the science education components of the core curriculum content standards as established by law.

The amount hereinabove appropriated for the Governor's Literacy Initiative shall be used for a grant for the Learning Through Listening program at the New Jersey Unit of Learning Ally.

The amount hereinabove appropriated for the Education Reform Implementation Grant Program shall be used by the Commissioner of Education to establish a competitive grant program to award grants to school districts implementing education reform initiatives. No more than $1,250,000 shall be awarded to grant recipient school districts to provide professional development opportunities consistent with the provisions of P.L.2012, c.30 (C.18A:6-119 et seq.). No more than $1,250,000 shall be awarded to grant recipients to school districts to prepare for the implementation of assessments developed by the Partnership for the Assessment of Readiness for College and Careers. No school district shall receive grants totaling more than $200,000.
34. EDUCATION

30. EDUCATIONAL, CULTURAL, AND INTELLECTUAL DEVELOPMENT

34. EDUCATIONAL SUPPORT SERVICES

Language -- State Aid -- Property Tax Relief Fund
15-495-034-5094-001 5094-045-30R0-0-60 Such additional sums as may be required for "Teachers" Pension and Annuity Fund -- Post Retirement Medical are appropriated, as the Director of the Division of Budget and Accounting shall determine.

15-495-034-5094-003 5094-045-35R0-0-60 Notwithstanding the provisions of any law or regulation to the contrary, of the amount hereinabove appropriated for Social Security Tax, there is appropriated such amounts, as determined by the Director of the Division of Budget and Accounting, to make payments on behalf of school districts that do not receive sufficient State formula aid payments under this act, for amounts due and owing to the State including out-of-district placements and such amounts shall be recognized by the school district as State revenue.

15-495-034-5094-003 5094-045-30R0-0-40 In addition to the amounts hereinabove appropriated for Social Security Tax, there are appropriated such sums as are required for payment of Social Security Taxes on behalf of members of the Teachers' Pension and Annuity Fund.

15-495-034-5094-004 5094-045-39R0-0-60 Such additional sums as may be required for the Teachers' Pension and Annuity Fund -- Non-contributory Insurance and Post Retirement Medical Other Than TPAP are appropriated, as the Director of the Division of Budget and Accounting shall determine.

15-495-034-5094-006 5094-045-39R0-0-60

35. EDUCATION ADMINISTRATION AND MANAGEMENT

99. ADMINISTRATION AND SUPPORT SERVICES

5090. DIVISION OF EXECUTIVE SERVICES

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPB Account No.</th>
<th>Direct State Services (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-100-034-5090-001</td>
<td>5090-100-9900-0-12</td>
<td>Personal Services: Salaries and Wages .................. (3,817)</td>
</tr>
<tr>
<td>15-100-034-5090-002</td>
<td>5090-100-9900-0-2</td>
<td>Materials and Supplies ................................... (57)</td>
</tr>
<tr>
<td>15-100-034-5090-003</td>
<td>5090-100-9900-0-3</td>
<td>Services Other Than Personal ............................... (659)</td>
</tr>
<tr>
<td>15-100-034-5090-004</td>
<td>5090-100-9900-0-4</td>
<td>Maintenance and Fixed Charges .............................. (4)</td>
</tr>
<tr>
<td>15-100-034-5090-008</td>
<td>5090-100-9900-0-5</td>
<td>State Board of Education Expenses ........................ (65)</td>
</tr>
</tbody>
</table>

Total Appropriation, Division of Executive Services .......................................................... 4,012

5092. PERFORMANCE AND AUDITING

41. DATA, RESEARCH EVALUATION AND REPORTING

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPB Account No.</th>
<th>Direct State Services (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-100-034-5092-001</td>
<td>5092-100-4100-0-12</td>
<td>Personal Services: Salaries and Wages .................. (718)</td>
</tr>
<tr>
<td>15-100-034-5092-002</td>
<td>5092-100-4100-0-2</td>
<td>Materials and Supplies ................................... (20)</td>
</tr>
<tr>
<td>15-100-034-5092-003</td>
<td>5092-100-4100-0-3</td>
<td>Services Other Than Personal ............................... (110)</td>
</tr>
</tbody>
</table>

Total Appropriation, Data, Research Evaluation and Reporting .............................................. 848

43. OFFICE OF FISCAL ACCOUNTABILITY AND COMPLIANCE

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPB Account No.</th>
<th>Direct State Services (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-100-034-5092-001</td>
<td>5092-100-4300-0-12</td>
<td>Personal Services: Salaries and Wages .................. (2,250)</td>
</tr>
<tr>
<td>15-100-034-5092-002</td>
<td>5092-100-4300-0-2</td>
<td>Materials and Supplies ................................... (19)</td>
</tr>
<tr>
<td>15-100-034-5092-003</td>
<td>5092-100-4300-0-3</td>
<td>Services Other Than Personal ............................... (50)</td>
</tr>
<tr>
<td>15-100-034-5092-004</td>
<td>5092-100-4300-0-4</td>
<td>Maintenance and Fixed Charges .............................. (30)</td>
</tr>
<tr>
<td>15-100-034-5092-012</td>
<td>5092-100-4300-0-5</td>
<td>Special Purpose: Internal Auditing ........................ (598)</td>
</tr>
</tbody>
</table>

Total Appropriation, Office of Fiscal Accountability and Compliance .................................... 2,867

Total Appropriation, Performance and Auditing .......................................................... 3,715
### 28. County Boards of Taxation

<table>
<thead>
<tr>
<th>NICES Account No.</th>
<th>IPB Account No.</th>
<th>County Boards of Taxation (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>13-160-081-2078-016</td>
<td>2076-150-200018-60</td>
<td>1,903</td>
</tr>
</tbody>
</table>

**Total Appropriation, County Boards of Taxation**

- 1,903

### 39. Locally Provided Assistance

<table>
<thead>
<tr>
<th>NICES Account No.</th>
<th>IPB Account No.</th>
<th>State Aid (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>13-160-081-2078-020</td>
<td>2076-150-200018-60</td>
<td>South Jersey Port Corporation Debt Service Reserve Fund : 19,419</td>
</tr>
<tr>
<td>13-160-081-2078-026</td>
<td>2076-150-200018-60</td>
<td>South Jersey Port Corporation Property Tax Reserve Fund : 5,101</td>
</tr>
<tr>
<td>13-160-081-2078-033</td>
<td>2076-150-200018-60</td>
<td>Highlands Protection Fund - Planning Grants : 2,182</td>
</tr>
<tr>
<td>13-160-081-2078-034</td>
<td>2076-150-200018-60</td>
<td>Highlands Protection Fund - Watershed Mitigation Offset Aid : 2,218</td>
</tr>
<tr>
<td>13-160-081-2078-043</td>
<td>2076-150-200018-60</td>
<td>Public Library Project Fund : 3,751</td>
</tr>
</tbody>
</table>

**Total Appropriation, Locally Provided Assistance**

- 32,671

### 33. Homestead Exemptions

<table>
<thead>
<tr>
<th>NICES Account No.</th>
<th>IPB Account No.</th>
<th>State Aid (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>13-495-081-2078-017</td>
<td>2076-495-130020-61</td>
<td>Homestead Benefit Program (PTRO) : 374,200</td>
</tr>
<tr>
<td>13-495-082-2078-007</td>
<td>2076-495-130060-61</td>
<td>Senior and Disabled Citizens' Property Tax Freeze (PTRO) : 199,600</td>
</tr>
</tbody>
</table>

**Total Appropriation, Homestead Exemptions**

- 573,800

### 34. Senior and Disabled Citizens' and Veterans' Property Tax Deductions

<table>
<thead>
<tr>
<th>NICES Account No.</th>
<th>IPB Account No.</th>
<th>State Aid (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>13-495-081-2078-004</td>
<td>2076-495-340456-60</td>
<td>Senior and Disabled Citizens' Property Tax Deductions (PTRF) : 13,200</td>
</tr>
<tr>
<td>13-495-082-2078-005</td>
<td>2076-495-340456-60</td>
<td>Veterans' Property Tax Deductions (PTRF) : 56,300</td>
</tr>
</tbody>
</table>

**Total Appropriation, Senior and Disabled Citizens' and Veterans' Property Tax Deductions**

- 69,500

### 35. Police and Firemen's Retirement System

<table>
<thead>
<tr>
<th>NICES Account No.</th>
<th>IPB Account No.</th>
<th>State Aid (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>13-495-081-2078-010</td>
<td>2076-495-350011-60</td>
<td>Debt Service on Pension Obligation Bonds (PTRF) : 17,872</td>
</tr>
<tr>
<td>13-495-081-2078-011</td>
<td>2076-495-350011-60</td>
<td>Police and Firemen's Retirement System - Post Retirement Medical (PTRF) : 45,294</td>
</tr>
<tr>
<td>13-495-082-2078-012</td>
<td>2076-495-356558-60</td>
<td>Police and Firemen's Retirement System (PTRF) : 28,620</td>
</tr>
<tr>
<td>13-495-082-2078-019</td>
<td>2076-495-356570-60</td>
<td>Police and Firemen's Retirement System (P.L.1979, c.109) (PTRF) : 37,603</td>
</tr>
</tbody>
</table>

**Total Appropriation, Police and Firemen's Retirement System**

- 129,379

**Total Appropriation, State Subsidies and Services:**

- 807,253
  - (From General Fund) 24,574
  - (From Property Tax Relief Fund) 772,679

**Total Appropriation, State Subsidies and Financial Aid:**

- 807,253
  - (From General Fund) 24,574
  - (From Property Tax Relief Fund) 772,679
70. GOVERNMENT DIRECTION, MANAGEMENT, AND CONTROL
75. STATE SUBSIDIES AND FINANCIAL AID

Language -- Grants-In-Aid - Property Tax Relief Fund

15-495-082-2078-017 2078-495-330200-61

The amount hereinabove appropriated for the Homestead Benefit Program shall be available to provide homestead benefits only to eligible homeowners pursuant to the provisions of section 3 of P.L. 1990, c.61 (C:54:4-5.9) as amended by P.L. 2004, c.40 and by P.L. 2007, c.62, as may be amended from time to time except that, notwithstanding the provisions of such laws to the contrary, (i) residents who are 65 years of age or older at the close of the tax year, or residents who are allowed to claim a personal deduction as a blind or disabled taxpayer pursuant to subsection b. of N.J.S.54A:3-1, with (a) gross income in excess of $150,000 for tax year 2012 are excluded from the program; (b) gross income in excess of $100,000 but not in excess of $150,000 for tax year 2012 are eligible for a benefit in the amount of 5% of the first $10,000 of property taxes paid; and (c) gross income not in excess of $100,000 for tax year 2012 are eligible for a benefit in the amount of 10% of the first $10,000 of property taxes paid; (ii) residents who are 65 years of age or older at the close of the tax year, or residents who are allowed to claim a personal deduction as a blind or disabled taxpayer pursuant to subsection b. of N.J.S.54A:3-1, with (a) gross income in excess of $150,000 for tax year 2012 are excluded from the program; (b) gross income in excess of $50,000 but not in excess of $75,000 for tax year 2012 are eligible for a benefit in the amount of 6.67% of the first $10,000 of property taxes paid; and (c) gross income not in excess of $50,000 for tax year 2012 are eligible for a benefit in the amount of 10% of the first $10,000 of property taxes paid. These benefits listed pursuant to this paragraph will be calculated based on the 2006 property tax amounts assessed as of the date that would have been assessed on the October 1, 2012 principal amount of the Homestead Benefit Program provided to eligible applicants in a given State Fiscal Year shall not exceed the homestead rebate amount paid to such eligible applicants for tax year 2000. The above may affect an applicant’s filing characteristics. The homestead benefit shall be paid in whole, subject to the approval of the Director of the Division of Budget and Accounting.

15-495-082-2078-017 2078-495-200200-61

From the amount hereinabove appropriated for the Homestead Benefit Program, there are appropriated such amounts as may be necessary for the administration of the program, subject to the approval of the Director of the Division of Budget and Accounting.

15-495-082-2078-017 2078-495-350200-61

From the amount hereinabove appropriated for the Homestead Benefit Program, there are appropriated such amounts as may be necessary for the administration of the program, subject to the approval of the Director of the Division of Budget and Accounting.

15-495-082-2078-017 2078-495-330200-61

From the amount hereinabove appropriated for the Homestead Benefit Program, there are appropriated such amounts as may be necessary for the administration of the program, subject to the approval of the Director of the Division of Budget and Accounting.

15-495-082-2078-007 2078-495-250006-61

Notwithstanding the provisions of P.L. 1997, c.348 (C:54:4-8.67 et seq.), the amount hereinabove appropriated for Senior and Disabled Citizens’ Property Tax Freeze, and any additional amounts which may be required for this purpose, is appropriated from the Property Tax Relief Fund.

15-495-082-2078-007 2078-495-350000-61

Notwithstanding the provisions of any law or regulation to the contrary, the amount hereinabove appropriated for Senior and Disabled Citizens’ Property Tax Freeze is subject to the following condition: eligibility for the property tax reimbursement program shall be determined pursuant to section 1 of P.L. 1997, c.348 (C:54:4-8.67), except that any citizen with an annual income of not more than $70,000 shall not be eligible to receive a property tax reimbursement benefit payment in the current fiscal year.

Language -- State Aid - General Fund

15-100-082-2078-020 2078-150-290010-60

There are appropriated such additional amounts as may be certified to the Governor by the South Jersey Port Corporation as necessary to meet the requirements of the South Jersey Port Corporation Debt Service Reserve Fund under section 14 of P.L. 1990, c.68 (C:42A:14-9) and the South Jersey Port Corporation Property Tax Reserve Fund under section 201 of P.L. 1998, c.69 (C:42A:14-20), subject to the approval of the Director of the Division of Budget and Accounting.

15-100-082-2078-032 2078-150-290210-60

The amounts hereinabove appropriated for the Highlands Protection Fund are payable from the receipt of the portion of the realty transfer fee directed to be credited to the Highlands Protection Fund and the unexpended balances at the end of the preceding fiscal year in the Highlands Protection Fund accounts are appropriated, subject to the approval of the Director of the Division of Budget and Accounting.

15-100-082-2078-033 2078-150-290220-60

The amounts hereinabove appropriated for the Highlands Protection Fund are payable from the receipt of the portion of the realty transfer fee directed to be credited to the Highlands Protection Fund and the unexpended balances at the end of the preceding fiscal year in the Highlands Protection Fund accounts are appropriated, subject to the approval of the Director of the Division of Budget and Accounting.

15-100-082-2078-034 2078-150-290230-60

The amounts hereinabove appropriated for the Highlands Protection Fund are payable from the receipt of the portion of the realty transfer fee directed to be credited to the Highlands Protection Fund and the unexpended balances at the end of the preceding fiscal year in the Highlands Protection Fund accounts are appropriated, subject to the approval of the Director of the Division of Budget and Accounting.

15-100-082-2078-035 2078-150-290240-60

The amounts hereinabove appropriated for the Highlands Protection Fund are payable from the receipt of the portion of the realty transfer fee directed to be credited to the Highlands Protection Fund and the unexpended balances at the end of the preceding fiscal year in the Highlands Protection Fund accounts are appropriated, subject to the approval of the Director of the Division of Budget and Accounting.

15-100-082-2078-019 2078-150-296680-60

The amounts hereinabove appropriated for the Highlands Protection Fund are payable from the receipt of the portion of the realty transfer fee directed to be credited to the Highlands Protection Fund and the unexpended balances at the end of the preceding fiscal year in the Highlands Protection Fund accounts are appropriated, subject to the approval of the Director of the Division of Budget and Accounting.

15-100-082-2078-019 2078-150-246680-60

The amount hereinabove appropriated for Solid Waste Management - County Environmental Investment Aid is appropriated to subsidize county and county authority debt service payments for environmental investments incurred and other repayment obligations owed pursuant to the “Solid Waste Management Act,” P.L. 1979, c.39 (C:13:1E-1 et seq.) and the “Solid Waste Utility Control Act,” P.L. 1970, c.49 (C:48:13A-1 et seq.) as determined by the State Treasurer based upon the need for such financial assistance after taking into account all financial resources available or attributable to pay such debt service and such other repayment obligations. Such additional sums as may be necessary shall be appropriated subject to the approval of the Director of the Division of Budget and Accounting and shall be provided upon such terms and conditions as the State Treasurer may determine. The unexpended balances at the end of the preceding fiscal year are appropriated, subject to the approval of the Director of the Division of Budget and Accounting.

Pa469
Notwithstanding the provisions of the "Corporation Business Tax Act (1945)," P.L.1945, c.162 (C.54:10A-1 et seq.), the amount apportioned to the several counties of the State shall not be distributed and shall be anticipated as revenue for general State purposes.

Notwithstanding the provisions of the "Corporation Business Tax Act (1945)," P.L.1945, c.162 (C.54:10A-1 et seq.), the amount collected from banking corporations pursuant to the "Corporation Business Tax Act (1945)" shall not be distributed to the counties and municipalities and shall be anticipated as revenue for general State purposes.

There is appropriated from the Energy Tax Receipts Property Tax Relief Fund the amount of $788,492,000 and an amount not to exceed $325,174,000 from Consolidated Municipal Property Tax Relief Aid is appropriated and shall be allocated to municipalities in accordance with the provisions of subsection b. of section 2 of P.L.1997, c.167 (C.52:27D-439), provided, however, that from the amounts hereinabove appropriated, each municipality shall receive such additional amounts from the Energy Tax Receipts Property Tax Relief Fund as provided in the previous fiscal year. Each municipality that receives an allocation from the amount so transferred from the Consolidated Municipal Property Tax Relief Aid program shall have its allocation from the Consolidated Municipal Property Tax Relief Aid program reduced by the same amount.

Notwithstanding the provisions of paragraph (1) of subsection c. of section 2 of P.L.1997, c.167 (C.52:27D-439) or any other law or regulation to the contrary, the amount hereinabove appropriated for Energy Tax Receipts Property Tax Relief Fund payments shall be distributed on the following schedule: on or before August 1, 45% of the total amount due; September 1, 30% of the total amount due; October 1, 15% of the total amount due; November 1, 5% of the total amount due; December 1 for municipalities operating under a calendar fiscal year; September 1 for municipalities operating under a fiscal year; September 1 for municipalities operating under the State fiscal year, 5% of the total amount due.

Notwithstanding the provisions of any law or regulation to the contrary, the release of the final 5% or $500, whichever is greater, of the total annual amount due for the current fiscal year from the Energy Tax Receipts Property Tax Relief Fund to municipalities is subject to the following conditions: the municipality shall submit to the Director of the Division of Local Government Services a report describing the municipality's compliance with the "Best Practices Inventory" established by the Director of the Division of Local Government Services, and shall receive at least a minimum score on such inventory as determined by the Director of the Division of Local Government Services; provided, however, that the Director may take into account the particular circumstances of a municipality in computing such score. In preparing the Best Practices Inventory, the Director shall identify best municipal practices in the areas of general administration, financial management, and operational activities as well as the particular circumstances of a municipality, in determining the minimum score acceptable for the release of the final 5% or $500, whichever is greater, of the total annual amount due for the current fiscal year, but in no event shall amounts be withheld with respect to municipal practices occurring prior to the issuance of the Best Practices Inventory unless related to a municipal practice identified in the Best Practices Inventory established in the previous fiscal year.

There is appropriated from taxes collected from certain insurance companies, pursuant to the Insurance Tax Act, so much as may be required for payments to counties pursuant to P.L.1945, c.132 (C.54:18A-1 et seq.).

The unexpended balance of the amount paid to counties pursuant to P.L.1948, c.5 (C.54:30A-49 et seq.) shall lapse.

The Director of the Division of Budget and Accounting shall reduce amounts provided to any municipality from the amount hereinabove appropriated for the difference, if any, between pension obligation savings, and the amount of Consolidated Municipal Property Tax Relief Aid payable to such municipality.

In addition to the amount hereinabove appropriated for Senior and Disabled Citizens' Property Tax Deductions and Veterans' Property Tax Deductions, there are appropriated from the Property Tax Relief Fund such additional amounts as may be required for State reimbursement to municipalities for senior and disabled citizens' and veterans' property tax deductions, subject to the approval of the Director of the Division of Budget and Accounting. Further, the Department of the Treasury, after notification to the Joint Budget Oversight Committee, may transfer funds as necessary between the Senior and Disabled Citizens' Property Tax Deduction account and the Veterans' Property Tax Deduction account, subject to the approval of the Director of the Division of Budget and Accounting.

In addition to the amount hereinabove appropriated for Debt Service on Pension Obligation Bonds to make payments under the State Treasurer's contracts authorized pursuant to section 6 of P.L.1997, c.114 (C.54:11B-7.5), there are appropriated such additional amounts as the Director of the Division of Budget and Accounting shall determine are required to pay all amounts due from the State pursuant to such contracts.

Such additional amounts as may be required for Police and Firemen's Retirement System - Post Retirement Medical are appropriated, as the Director of the Division of Budget and Accounting shall determine.
### 94. INTERDEPARTMENTAL ACCOUNTS

#### 70. GOVERNMENT DIRECTION, MANAGEMENT, AND CONTROL

#### 74. GENERAL GOVERNMENT SERVICES

<table>
<thead>
<tr>
<th>NICFS Account No.</th>
<th>IPB Account No.</th>
<th>Direct State Services</th>
<th>(thousands of dollars)</th>
</tr>
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<tbody>
<tr>
<td>15-100-004-9410-006</td>
<td>9410-100-03200-5</td>
<td>Public Employees' Retirement System</td>
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<td>Public Employees' Retirement System - Post Retirement Medical</td>
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<td>Police and Firemen's Retirement System - Non-contributory Insurance</td>
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<td>Police and Firemen's Retirement System (EL 1979, c.109)</td>
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<td>15-100-004-9410-015</td>
<td>9410-100-03228-5</td>
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<td>Judicial Retirement System - Non-contributory Insurance</td>
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<td>15-100-004-9410-016</td>
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<td>Teachers' Pension and Annuity Fund</td>
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<td>Teachers' Pension and Annuity Fund - Post Retirement Medical-State</td>
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<td>Teachers' Pension and Annuity Fund - Non-contributory Insurance</td>
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<td>Pension Adjustment Program</td>
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<td>15-100-004-9410-002</td>
<td>9410-100-03280-5</td>
<td>Veterans Act Pensions</td>
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<td>15-100-004-9410-106</td>
<td>9410-100-03310-5</td>
<td>Debt Service on Pension Obligation Bonds</td>
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<tr>
<td>15-100-004-9410-155</td>
<td>9410-100-033120-5</td>
<td>Volunteer Emergency Survivor Benefit</td>
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<td>15-100-004-9410-011</td>
<td>9410-100-03320-5</td>
<td>State Employees' Health Benefits</td>
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<tr>
<td>15-100-004-9410-156</td>
<td>9410-100-03320-5</td>
<td>Other Pension Systems-Post Retirement Medical</td>
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<td>State Employees' Prescription Drug Program</td>
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<td>15-100-004-9410-010</td>
<td>9410-100-03340-5</td>
<td>State Employees' Dental Program - Shared Cost</td>
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<td>15-100-004-9410-022</td>
<td>9410-100-03330-5</td>
<td>State Employees' Vision Care Program</td>
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<tr>
<td>15-100-004-9410-171</td>
<td>9410-100-03310-5</td>
<td>Affordable Care Act Fees</td>
<td>12,897</td>
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<tr>
<td>15-100-004-9410-107</td>
<td>9410-100-03300-5</td>
<td>Social Security Tax - State</td>
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<tr>
<td>15-100-004-9410-018</td>
<td>9410-100-03300-5</td>
<td>Temporary Disability Insurance Liability</td>
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<tr>
<td>15-100-004-9410-017</td>
<td>9410-100-03300-5</td>
<td>Unemployment Insurance Liability</td>
<td>8,746</td>
</tr>
</tbody>
</table>

Subtotal Appropriations, Direct State Services: 2,169,883
### 94. INTERDEPARTMENTAL ACCOUNTS

#### 70. GOVERNMENT DIRECTION, MANAGEMENT, AND CONTROL

#### 74. GENERAL GOVERNMENT SERVICES

<table>
<thead>
<tr>
<th>Account No.</th>
<th>Description</th>
<th>Amount (thousands of dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>15-100-001-010-130</td>
<td>Public Employees' Retirement System</td>
<td>14,565</td>
</tr>
<tr>
<td>15-100-001-010-153</td>
<td>Public Employees' Retirement System - Post Retirement Medical</td>
<td>56,728</td>
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<tr>
<td>15-100-001-010-165</td>
<td>Public Employees' Retirement System - Non-contributory Insurance</td>
<td>2,859</td>
</tr>
<tr>
<td>15-100-001-010-131</td>
<td>Police and Firemen's Retirement System</td>
<td>4,492</td>
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<tr>
<td>15-100-001-010-166</td>
<td>Police and Firemen's Retirement System - Non-contributory Insurance</td>
<td>287</td>
</tr>
<tr>
<td>15-100-001-010-132</td>
<td>Alternate Pension System - Employer Contributions</td>
<td>145,547</td>
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<td>15-100-001-010-167</td>
<td>Teacher's Pension and Annuity Fund</td>
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<td>15-100-001-010-133</td>
<td>Teacher's Pension and Annuity Fund - Post Retirement Medical</td>
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<tr>
<td>15-100-001-010-141</td>
<td>Debt Service on Pension Obligation Bonds</td>
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<tr>
<td>15-100-001-010-124</td>
<td>State Employees' Health Benefits</td>
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<td>15-100-001-010-158</td>
<td>Other Pension Systems - Post Retirement Medical</td>
<td>101,130</td>
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<tr>
<td>15-100-001-010-135</td>
<td>State Employees' Prescription Drug Program</td>
<td>10,578</td>
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<td>15-100-001-010-136</td>
<td>State Employees' Dental Program - Shared Cost</td>
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<td>15-100-001-010-172</td>
<td>Affordable Care Act Fees</td>
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<td>Social Security Tax - State</td>
<td>6,877</td>
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<td>15-100-001-010-138</td>
<td>Temporary Disability Insurance Liability</td>
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<tr>
<td>15-100-001-010-139</td>
<td>Unemployment Insurance Liability</td>
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</tr>
</tbody>
</table>

**Subtotal Appropriation, Grants-in-Aid:**

**Total Appropriation, Employee Benefits:** 2,124,103

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**Language - Direct State Services - General Fund**

Such additional amounts as may be required for Public Employees' Retirement System - Post Retirement Medical, Public Employees' Retirement System - Non-contributory Insurance, Police and Firemen's Retirement System - Non-contributory Insurance, Alternate Benefit Program - Employer Contributions, Alternate Benefit Program - Non-contributory Insurance, Defined Contribution Retirement Program, Defined Contributions Retirement Program - Non-contributory Insurance, Teacher's Pension and Annuity Fund - Post Retirement Medical, Teacher's Pension and Annuity Fund - Non-contributory Insurance, State Police Retirement System - Non-contributory Insurance, Judicial Retirement System - Non-contributory Insurance, State Employees' Health Benefits, Cuban Pension Systems - Post Retirement Medical, Medical Employees' Prescription Drug Program, State Employees' Dental Program - Shared Cost, State Employees' Vision Care Program, Affordable Care Act Fees, Social Security Tax - State, Temporary Disability Insurance Liability, and Unemployment Insurance Liability are appropriated, as directed by the Division of Budget and Accounting, shall determine.

No amounts hereinabove appropriated shall be used to provide additional health insurance coverage to a State or local elected official, unless such official receives health insurance coverage as a result of holding another public office or employment.

Notwithstanding the provisions of the "Pension Adjustment Act," P.L. 1958, c.143 (C:43:B-1 et seq.), pension adjustment benefits for State members and beneficiaries of the Consolidated Police and Firemen's Pension Fund, Prison Officers' Pension Fund, and Central Pension Fund shall be paid by the respective pension fund. The amounts hereinabove appropriated for the Pension Adjustment Fund for these benefits shall be paid to the Pension Adjustment Fund.

In addition to the amount hereinabove appropriated for Debt Service on Pension Obligation Bonds to make payments under the State Treasurer's contracts authorized pursuant to section 6 of P.L. 1997, c.114 (C:34:18-1750), there are appropriated such additional amounts as the Director of the Division of Budget and Accounting shall determine are required to pay all amounts due from the State pursuant to such contracts.
EXHIBIT "AA"
NEW YORK—(BUSINESS WIRE)—Fitch Ratings has assigned an 'A-' rating to the following New Jersey Educational Facilities Authority (NJEFA) bonds:

--$220 million higher education facilities trust fund bonds, series 2014.

The bonds are expected to sell via competitive bid on Sept. 18 2014.

In addition, Fitch has downgraded the following ratings for the state of New Jersey:

--$2.16 billion general obligation (GO) bonds to 'A' from 'A+';

--$940.2 million Garden State Preservation Trust bonds to 'A' from 'A+';

--Approximately $33.5 billion of state obligations secured by the state's annual appropriation pledge as detailed at the end of this release to 'A-' from 'A';

--The program ratings assigned to New Jersey Municipal Qualified Bonds and bonds secured by the New Jersey School Bond Reserve (New Jersey School Credit Enhancement Program) to 'A-' from 'A'.

The Rating Outlook remains Negative.

SECURITY

The bonds are special, limited obligations of the NJEFA, secured by payments to the authority from the state equal to principal and interest on the bonds, subject to annual appropriation.

Appropriation bonds, certificates of participation, and Garden State Preservation Trust revenue bonds are secured by annual state legislative appropriations, and in some cases, certain defined pledged revenue streams.

General obligations of the state are secured by the full faith and credit of the state.

KEY RATING DRIVERS

GO RATING DOWNGRADE: The downgrade to 'A' of New Jersey's GO bonds incorporates the absence of long-term, fiscally sustainable solutions to close identified budget gaps in fiscal years 2014 and 2015. Following significant revenue underperformance, the state relied upon the repudiation of its statutory contribution requirements to the pension systems to return to budgetary balance, exacerbating a key credit weakness. The resurgence of sizable one-time measures to balance its operating budgets at a time of economic recovery, driven by past overly optimistic revenue forecasts and maintenance of extremely narrow financial reserves, illustrates the fiscal pressure the state faces. New Jersey's economic performance continues to lag that of the nation and a multitude of long-term spending demands are expected to prolong the achievement of sound financial operations.
APPROPRIATION OBLIGATIONS OF THE STATE: The downgrade to 'A-' of the state's appropriation-backed obligations (including those issued by the NJEFA), one notch below the state's GO bond rating, reflects the linkage to the state's GO bond rating due to the requirement for annual appropriations for debt service.

NEGATIVE OUTLOOK: Maintenance of the Negative Rating Outlook Incorporates Fitch's concern that there is considerable risk that state actions to address near-term budgetary and pension challenges may leave unaddressed the state's longer-term structural and liability challenges, particularly given the state's lagging economic and revenue performance and narrow liquidity.

LONG-TERM LIABILITIES CONSIDERABLE: Above-average state debt obligations are compounded by significant and growing funding needs for the state's unfunded retirement liabilities. Continued pension funded ratio deterioration is projected through the medium term and full actuarial funding of the required contributions is several years off.

WEALTHY ECONOMY AND LAGGING RECOVERY: New Jersey benefits from a wealthy populace and a broad and diverse economy. However, the state's economic performance has lagged the nation in recovery from the recent recession, with improvement in 2013 trailing off at the close of the year, and very slow year over year (yoy) employment growth continuing through 2014.

MINIMAL CASH BALANCES RESULT IN LIMITED OPERATING FLEXIBILITY: Minimal cash balances have been maintained in recent years, providing limited flexibility to absorb unforeseen needs or revenue underperformance.

BROAD EXPENDITURE REDUCTION AUTHORITY: The governor has strong executive powers to implement any necessary expenditure reductions to balance the budget and the state has a consistent history of doing so; however, options have become more limited as the state's fixed cost burden grows.

RATING SENSITIVITIES

EFFECTIVE MANAGEMENT OF BUDGET CHALLENGES: Continued deterioration in the state's budgetary flexibility or reserves or a failure to adequately provide for its liabilities, could lead to a downgrade.

APPROPRIATION RATINGS LINKED TO STATE: The annual appropriation ratings and other ratings noted at the end of the release are sensitive to shifts in the state's GO credit rating to which they are linked.

CREDIT PROFILE

The downgrade of New Jersey's GO rating to 'A' from 'A+' incorporates the absence of long-term, fiscally sustainable solutions to close identified budget gaps in fiscal years 2014 and 2015. Achieving budgetary balance, following significant revenue underperformance at a time of national economic recovery, relied upon the state repudiating its planned statutory contribution to the pension systems. The downgrade also incorporates the resurgence of sizable one-time measures to balance its operating budgets, driven by overly optimistic revenue forecasts and maintenance of extremely narrow financial reserves.

The state's economic performance continues to lag that of the nation as it emerges from the recent recession and it faces a multitude of long-term spending pressures which are expected to prolong its achievement of sound financial operations. In Fitch's view, Financial operations have also been challenged by a multitude of long-term spending pressures including significant unfunded pension and employee benefit obligations. Additionally, the state maintains a very weak liquidity position, providing little maneuverability in its budgetary operations.

New Jersey benefits from high wealth levels and a broad economy; these positives are offset, however, by a high debt burden and sizable unfunded retiree liabilities. Despite passage of pension and benefits reform legislation in 2011 which restrained future growth in the state's accumulated liabilities, continued pension funding-level
deterioration is projected through the medium term as the state's statutory plan phased in a return to full actuarial contributions over time. The state's suspension of its planned statutory contributions in fiscal years 2014 and 2015 is likely to further erode pension funded ratios. Fitch believes balancing the need for requisite pension system contributions with other long-term demands, such as infrastructure needs, property tax relief, and school funding will continue to prove difficult.

FINANCIAL OPERATIONS ARE STRUCTURALLY UNBALANCED

Projected revenues in the enacted budget for fiscal 2014 totaled $32.8 billion and incorporated growth from actual 2013 results, including: 7.7% growth in the personal income tax (PIT), 5.4% growth in the sales tax, 2.2% growth in the corporation business tax (CBT), and 76% ($168 million) growth in casino revenue resulting from the introduction of internet gaming tied to Atlantic City casinos. Given fiscal 2014 revenue underperformance through January 2014, the governor's proposed fiscal 2015 budget, released in February 2014, included a net $251 million negative revision to the fiscal 2014 revenue forecast. Factored into the revision was the expected receipt of one-time proceeds from a securitization of the state's remaining tobacco settlement revenues; the transaction brought a net $91.8 million into the general fund, without which the revenue gap would have been $342.7 million.

In addition to this revenue gap, in February the state incorporated $694 million of appropriation lapses from unexpended items, including about $94 million in pension savings from the combined effect of incorporating salary scale changes from recently adopted experience studies and a more favorable method of calculating the state's normal cost pension contributions. These lapses allowed the state to fund an increase in appropriations of $292 million for fiscal 2014.

An additional $807 million revenue gap, announced in April 2014, increased the size of the revenue shortfall for fiscal 2014 compared to the enacted budget to approximately $1.3 billion; approximately 3.9% of the state's operating budget. The state reported the shortfall was largely due to an approximate $700 million shortfall in PIT receipts for fiscal 2014. The revenue shortfall for fiscal 2014, when combined with other revenue and expenditure adjustments, created a $1.75 billion budget gap for fiscal 2015.

The governor proposed a $887 million reduction to the statutory $1.58 billion pension payment for fiscal 2014 as well as a $1.57 billion reduction from the statutory $2.25 billion pension payment for fiscal 2015 as the primary means of closing the newly-identified budget gaps. Despite legal challenge, the fiscal 2014 cut was upheld by a state superior court judge, who cited the state's emergency fiscal situation given the announcement of the gap late in the fiscal year; however, the judge did not rule on the proposed cut to the fiscal 2015 pension payment as the budget had not yet been enacted. The judge's ruling, while sustaining the cut to the pension payment in fiscal 2014, concurred with the plaintiffs' contention that pension benefits represent a contractual obligation of the state, paralleling another recent state court decision on pension benefits.

Including the $887 million reduction to the contribution for the state's pension systems, one-time actions in the fiscal 2014 operating budget ultimately totaled just over $3 billion; equal to 9.3% of the $33.2 billion operating budget. These included $92 million in tobacco securitization, an EDA bond refunding, tax policy and revenue initiatives, the change to the normal cost pension contribution, and various appropriation offsets.

A sharp disagreement arose between the New Jersey governor and legislature on how to close the budget gap for fiscal 2015. The disagreement resulted in the governor's line item veto of $1.57 billion from the $2.25 billion pension contribution for fiscal 2015 following the legislature's approval of personal income and business tax increases to cover the scheduled pension contribution. The governor vetoed the tax increases and reduced the pension contribution instead. The timeline for resolving litigation regarding the pension contribution cut for fiscal 2015 is not yet clear.

The fiscal 2015 enacted operating funds budget is 2.1% below the final estimated budget for fiscal 2014. Appropriations have been reduced by $692 million from fiscal 2014 and total just over $32.5 billion. Revenues in support of the budget are forecast to increase by 3.5%, including; a 5.5% increase in sales tax revenue, a 4.8%
Increase in the PIT, a 6.5% increase in the CBT, and a 17.6% ($40 million) increase in casino revenues. One-time actions included in the budget are estimated to total $2.75 billion (8.5% of the fiscal 2015 operating budget) and include the $1.57 pension payment cut, $231 million in appropriation offsets, $324 million from the NJ Turnpike to offset appropriations to NJ Transit, and $391 million in debt restructuring. In Fitch's view, past state economic and revenue forecasts have been optimistic. The current economic and revenue forecast appears to closely match those of independent forecasters.

The state has indicated its intent to increase its ending fund balance to $388.5 million at the close of fiscal 2015; up from an estimated $300 million ending fund balance in fiscal 2014. Fitch believes this level of fund balance; 1.2% of operating revenue; would provide only limited operating flexibility in the event of future negative fiscal developments.

ECONOMIC GROWTH HAS LAGGED THE NATION

State employment growth during most of the last decade lagged the national experience, and while growth has returned following recessionary losses, the pace of expansion remains well below the national average. The state entered the recession with the nation in 2008 and its experience from 2008 to 2010 was similar, although the state recorded a decline of 1.2% in non-farm employment levels in 2010, higher than the 0.7% contraction seen nationally; growth in 2011 was essentially flat to 2010 and below the 1.2% national growth rate. Modest employment growth in both 2012 and 2013 of 1.1% was below the national 1.7% growth rate for both years.

Improved state yoy employment growth in the fall of 2013 trailed off at the year’s close and employment in July 2014 was a modest gain of 0.6% yoy as compared to 1.9% yoy national employment growth. State unemployment of 6.5% for July 2014 was solidly improved from the rate one year prior at 8.3%; however, the decline in the rate is likely attributable to a yoy decline in the workforce participation rate; the state’s civilian labor force declined by 43,500 and actual yoy employment increased by 32,000 in July.

New Jersey’s wealth levels are high, with 2013 per capita personal income equaling 126% of the national level, ranking it fourth among the states.

COMPARATIVELY HIGH LONG-TERM LIABILITIES

New Jersey’s debt levels are high for a U.S. state, and ongoing capital demands for school construction, environmental protection and transportation remain large. Net tax-supported debt as of June 30, 2014 equaled 7.4% of 2013 personal income as compared to a median of 2.6% for the states.

Unfunded pension liabilities attributable to the state are also well above average. Unfunded pension liabilities are expected to increase over the next several years absent additional reform measures and materially higher contributions than currently expected. Fitch expects the pension contribution increases, combined with expected annual increases in OPEB funding demands, to further strain the state’s operating budget.

For the public employees' retirement system (PERS) and the teachers' pension and annuity fund (TPAF), as of July 1, 2013, system wide reported funded ratios were 62.1% and 57.1%, respectively. Using Fitch's more conservative 7% discount rate assumption, the plans were 66.5% and 61.9% funded, respectively. As of July 1, 2013, the state portion of pension liabilities for PERS was 46% funded on a reported basis, or 41.8% using Fitch's more conservative 7% discount rate. On a combined basis, as of July 1, 2013, New Jersey's net tax-supported debt and adjusted, unfunded pension obligations attributable to the state, as adjusted for a 7% return assumption, totaled 18.5% of 2013 personal income, well above the 6.1% median for all U.S. states.

The governor has recently convened a special pension task force to propose options for additional pension reform. In delivering the budget proposal to the legislature, the governor acknowledged the sizable and increasing burden of pension contributions and recommended that additional, as yet unspecified, reform measures be considered in the current legislative session.
RELATED DEBT

The ratings on the following credits, which are linked to the state GO rating, have been downgraded as indicated. The Rating Outlook on all the bonds remains Negative.

- Approximately $13.5 billion New Jersey Economic Development Authority annual appropriation bonds to 'A-' from 'A';

- Approximately $14.8 billion New Jersey Transportation Trust Fund Authority annual appropriation bonds to 'A-' from 'A';

- Approximately $940 million Garden State Preservation Trust revenue bonds to 'A' from 'A+';

- Approximately $541.9 million New Jersey Building Authority annual appropriation bonds to 'A-' from 'A';

- Approximately $673.5 million New Jersey Educational Facilities Authority annual appropriation bonds to 'A-' from 'A';

- Approximately $703.5 million New Jersey Health Care Facilities Financing Authority annual appropriation bonds to 'A-' from 'A';

- Approximately $440.5 million New Jersey Sports and Exposition Authority annual appropriation bonds to 'A-' from 'A';

- Approximately $671.1 million of state of New Jersey certificates of participation to 'A-' from 'A';

- The program ratings assigned to New Jersey Municipal Qualified Bonds and bonds secured by the New Jersey School Bond Reserve (New Jersey School Credit Enhancement Program) to 'A-' from 'A'.

The 'A-' ratings for the state's appropriation obligations, one notch below the state's GO rating, reflects the requirement of annual legislative appropriations for debt service. The 'A' rating for the Garden State Preservation revenue bonds reflects that while annual legislative appropriation of dedicated sales tax revenue is necessary, the provision that if the legislature fails to make the appropriation, dedicated funds may not be for any other purpose, effectively eliminates the risk of non-appropriation in Fitch's opinion, allowing for a rating on par with the state's GO debt.

Additional information is available at www.fitchratings.com.

In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from IHS Global Insight.

Applicable Criteria and Related Research:

- 'Tax-Supported Rating Criteria' (Aug. 14, 2012);

- 'U.S. State Government Tax-Supported Rating Criteria' (Aug. 14, 2012);


- 'Fitch Revises Outlook on New Jersey GO and Appropriation Bond Ratings to Negative' (March 21, 2014).
Tax-Supported Rating Criteria


U.S. State Government Tax-Supported Rating Criteria


State of New Jersey


Additional Disclosure

Solicitation Status


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Contacts
Fitch Ratings
Primary Analyst
Marcy Block
Senior Director
+1-212-908-0239
Fitch Ratings, Inc.
33 Whitehall Street
New York, NY 10004
or
Secondary Analyst
Karen Krop
Senior Director
+1-212-908-0661
or
Committee Chairperson
Douglas Offerman
Senior Director
+1-212-908-0889
or
Media Relations
Elizabeth Fogerty, New York, +1-212-908-0526
elizabeth.fogerty@litchratings.com
New Jersey GO Debt Rating Lowered To 'A' From 'A+' On Rising Long-Term Liabilities

NEW YORK (Standard & Poor's) Sept. 10, 2014--Standard & Poor's Ratings Services has lowered its rating on New Jersey's general obligation (GO) bonds to 'A' from 'A+'. Standard & Poor's lowered its rating on New Jersey's appropriation-backed debt to 'A-' from 'A', and its rating on New Jersey's moral obligation debt to 'BBB' from 'BBB+'. Standard & Poor's also removed the ratings from CreditWatch with negative implications, where they had been placed June 2, 2014. The outlook is stable.

"The downgrade reflects our view that New Jersey will face increased long-term pressures in managing its long-term liabilities and that the revenue and expenditure misalignment will grow based on reduced funding of the state's unfunded actuarial accrued liability," said Standard & Poor's credit analyst John Sugden.

At the same time, Standard & Poor's assigned its 'A-' rating and stable outlook to New Jersey Educational Facilities Authority's higher education facilities trust funds, series 2014A. The trust fund bonds are secured by payments received by the authority pursuant to the Trust Fund Act. Payments are subject to appropriation by the New Jersey legislature in accordance with the trust fund act. The state is issuing the series 2014 trust fund bonds to fund capital improvement grants to certain public and private higher education institutions. The 'A-' rating reflects the appropriation risk associated with the bonds as well as the state's general creditworthiness.

The 'A' GO rating reflects our assessment of:
- A trend of structurally unbalanced budgets that include only normal cost funding of pension obligations and reliance on one-time measures that are contributing to additional pressure on future budgets;
- Lack of consensus among elected leaders on how to return to structural balance;
- A large and growing unfunded pension liability;
- Significant postemployment benefit obligations; and
- An above-average debt burden.

In our opinion, credit strengths include New Jersey's:
- Diverse economic base, which is showing signs of improvement, but has a
long way to go to full recovery;
- High wealth and incomes, which are still among the highest of the 50 states.

On May 21, the state identified an additional $1 billion, or 3.2% of budget, revenue shortfall for fiscal 2014 from the governor's February budget message. The state also reduced its revenue forecast for fiscal 2015 by $1.7 billion, or 5%, from the governor's fiscal 2015 budget message to account for lower baseline revenues and a reduction to the estimated growth rate to 3.9% from 5.8%. To offset these revenue reductions, the governor identified just over $1 billion in spending reductions for fiscal 2014 and $1.7 billion in fiscal 2015, tied primarily to a reduction in its pension contribution—a departure from the administration's own pension reform efforts. The governor has broad executive powers to reduce spending as necessary to maintain the budget in balance in 2014 and for fiscal 2015 used his veto power to reduce the pension funding and related revenue increase proposals included in the appropriations act by the legislature.

New Jersey continues to struggle with structural imbalance and the governor's decision to reduce pension contributions in fiscal 2014 and 2015 highlights the fact that the state lacks the revenues to comply with its own agreed-on contribution to the pension system. In our view, the governor's decision to delay pension funding, while providing the necessary tools for cash management and budget control, has significant negative implications for the state's liability profile. Pension funded levels, which were expected to decline until the state reached the full funding of annual required contribution (ARC), are now expected to decline much more significantly and place increased pressure on future funding requirements. The state's projections of declining funded levels assumed not only that the 2014 and 2015 payments would be made in accordance with the three-sevenths and four-sevenths requirements, but also that those funds, once invested by the pension system, would result in additional investment returns at 7.9%. Based on preliminary updated estimates, the state expects its pension funded level, absent any other action by the state, to decline to 80.24% by 2019. This, however, assumes that New Jersey will resume payments on a four-seventh of ARC basis starting in fiscal 2016 and continuing through 2019. Revenues in fiscal 2016 would have to increase by approximately 5% from estimated revenues in fiscal 2015, just to fund the increased pension payment.

Although in his State of the State and budget messages, the governor called for additional pension reform efforts, there has been no formal proposal released. In August 2014, the governor created and appointed members to a commission (New Jersey Pension and Health Benefit Study Commission) to provide recommendations on how to achieve sustainability of pension and health benefits in the state. The governor vetoed the legislature's proposals to increase taxes to continue to fund pensions; therefore, it is likely that any pension reform proposals will be primarily focused on changes to retirement and health benefits, rather than on increased funding. In the absence of consensus between the legislative and executive branches, any type of pension solution is likely to be delayed and result in mounting financial pressures for the state in the long term.
The stable outlook reflects our expectation that New Jersey will ultimately retain a strong ability to fund its debt obligations as they come due despite a likelihood, in our view, that its budget will continue to be structurally imbalanced and that reliance on one-time measures will remain at or close to current levels. The current rating also accommodates some additional deterioration in the state's pension funded levels, which we believe is likely given the state's demonstrated lack of commitment when it comes to funding its annual contributions. Beyond the two-year outlook horizon, the rating could come under renewed pressure if there is inaction by elected leaders to address long-term liabilities and the funded level of New Jersey's retiree liabilities continues to erode. More immediate pressure on the rating would likely be the result of unanticipated liquidity strain or if—within the next two years—the state's budget or liability situation weakened more than we currently anticipate. On the other hand, until the state implements fiscal reforms that bring its budgetary condition into structural alignment without relying on optimistic forecasting, we don't anticipate raising the rating. At this point, given its structural fiscal challenges, even if the economy and revenues were to match or outpace New Jersey's forecast, it's unlikely to result in a higher rating. Furthermore, we also expect that larger budget reserves and improved execution when it comes to retiree liability reform efforts would likely accompany improvement in the state's credit quality.

RELATED CRITERIA AND RESEARCH

Related Criteria
• USPF Criteria: State Ratings Methodology, Jan. 3, 2011
• USPF Criteria: Appropriation-Backed Obligations, June 13, 2007
• Criteria: Joint Support Criteria Update, April 22, 2009
• USPF Criteria: Financial Management Assessment, June 27, 2006
• USPF Criteria: Moral Obligation Bonds, June 27, 2006

Related Research
• U.S. State And Local Government Credit Conditions Forecast, July 8, 2014

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.

Media Contact:
Alex Ortolani, New York (1) 212-438-5054
alex.ortolani@standardandpoors.com

Analyst Contacts:
John A. Sugden, New York (1) 212-438-1678
David G. Hitchcock, New York (1) 212-438-2022
http://www.standardandpoors.com
EXHIBIT  "CC"
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LETTER FROM THE COMMISSION

COMMISSION MEMBERS
Thomas J. Healey
Margaret S. Berger
Tom Byrne
Raymond G. Chambers
Leonard W. Davis
Carl A. Hess
Ethan E. Kra
Kenneth F. Kunzman
Lawrence J. Sher
Raj Tatta

September 25, 2014

Executive Order No. 161 creating the New Jersey Pension and Health Benefit Study Commission was signed by Governor Christie on August 1, 2014. The Commission consists of ten members whose backgrounds are described in Appendix 1.

This Status Report ("Report"), dated September 25, 2014, examines the State of New Jersey’s existing pension and health benefit systems. Unlike some studies which have looked at these systems from a combined State and local perspective, this Report focuses on the elements for which the State bears financial responsibility. It examines the history and current challenges faced by these systems, and looks at the responses to similar challenges by other state government entities and comparable pension and health benefits in both the public and private sectors.

This Report is designed to be primarily factual and explanatory in nature. As we move forward to our final report, which will recommend solutions for dealing with these challenges, the Commission welcomes comment as to the current situation. We also encourage suggestions regarding pension and health benefit reforms that will strengthen the systems’ financial standing and reduce the cost to taxpayers of providing public employees and retirees with an appropriate level of benefits.

All are encouraged to use the Commission’s website to respond:
http://www.state.nj.us/treasury/pensionandbenefitcommission.shtml

This report is intended for educational and informational purposes. References to specific policymakers or companies have been included solely to advance these purposes and do not constitute an endorsement, sponsorship, or recommendation.

Status Report of the New Jersey Pension and Health Benefit Study Commission

Pa49C
I. EXECUTIVE SUMMARY

The public employee pension and health benefit systems of the State of New Jersey face problems that are dire and likely to worsen unless action is taken. This is a matter of pressing concern to the public employees and retirees who rely on these systems to protect their families' health and provide for retirement. These public servants are our neighbors, friends and families, and they play a vital role in preserving the security, safety and health of our State and in educating our children. The benefit commitments the State has made also play a critical role in attracting and maintaining a stable and highly-qualified public sector workforce, a matter of concern to all the citizens of the State who place their livelihoods and even their lives in the hands of State employees on matters ranging from license renewals to disaster relief.

Both public employees and taxpayers as a whole, however, have been poorly served by a long-standing and bipartisan tradition of increasing benefit levels without adequate funding. Successive Governors and State Legislatures have committed the State to providing these benefits based on relatively optimistic financial assumptions without adequate consideration of the long-term costs to taxpayers if economic reality were to fall short of these assumptions.

The broad parameters of the problem can be seen by comparing what the State actually spent on employee benefits in fiscal year ("FY") 2014 against what would have been required to meet in full its employee benefit obligations for that year.

2014 Pension and Health Benefit Spending by the State of New Jersey

<table>
<thead>
<tr>
<th>$ Millions</th>
<th>Actual Pension Spcending</th>
<th>Actual Health Benefit Spending</th>
<th>Unmet Pension Contribution</th>
<th>Minimum Requirement</th>
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</thead>
<tbody>
<tr>
<td>0</td>
<td>$696</td>
<td>$2,801</td>
<td>$2,995</td>
<td>$6,492</td>
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<tr>
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<tr>
<td>7,000</td>
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</table>

This $3 billion gap between the annual cost of benefits and the money allocated to pay for them will continue to grow in every budget for the foreseeable future unless significant action is taken.

In round numbers, the $700 million actual pension contribution and $2.8 billion health benefit payment amount to $3.5 billion in employee benefit spending by the State in FY 2014. This was over 10% of its $33 billion budget. It would have taken $6.5 billion, or 20% of the budget, to satisfy fully the funding obligation defined by statute. Unless the $3 billion gap between the cost of benefits at their current levels and the funds allocated to pay for them is reconciled by reducing costs and/or increasing funding, this gap will continue to grow in every budget for the foreseeable future.

The specific cause of the $3 billion gap in FY 2014 is that the State paid less than $700 million of the $3.7 billion it would have had to have paid to meet its statutory annual required contribution ("ARC")² to the pension funds for that year. Moreover, as discussed below, it should be understood that $3 billion represents a conservative estimate of the gap given the State's current pension

Status Report of the New Jersey Pension and Health Benefit Study Commission
obligations. There are substantial uncertainties underlying this projection. Under many scenarios, this contribution gap would be meaningfully larger, a consideration which bears upon the “Risk” discussion in Section VI of this Report.

The focus of reforms, however, cannot be limited to pensions. The State’s employee benefits obligation consists of pension and health care expenses. The State spent $2.8 billion on health benefits in FY 2014, and the cost of these benefits, which are high both in absolute terms and relative to what other public and private employers pay, has been growing faster than State revenues. It is crucial that these costs be controlled.

One particular element of health care expenses which is frequently overlooked but deserves closer consideration because of the demand it will place on future budgets is retiree health care costs. Government accounting rules require the costs of both pension and retiree health benefits to be recognized on the State’s financial statements as employees earn these benefits each year. However, unlike pensions, New Jersey, like most public and private sector employers, does not put money aside to pay for future retiree health benefits. The entire retiree health benefit obligation is left to be paid by future taxpayers as a pay-as-you-go expense. The size of this future obligation is substantial: it represents a $53 billion unfunded liability on top of the ever-growing cost of providing health benefits to current active employees.

Looked at together, the $37 billion unfunded portion of the total pension liability and the $53 billion unfunded retiree health obligation represent a $90 billion drain on future budgets. By improving funding levels and reducing benefit costs, it is possible to reduce the size of this future burden on taxpayers. If we do nothing, it will only grow.

The combined unfunded liability for pensions and retiree health benefits is $90 billion - almost three times the annual state budget.

This problem, which all major stakeholders had a role in creating, has immediate, real-world implications. In April and May 2014, Standard & Poor’s, Fitch and Moody’s each downgraded New Jersey’s general obligation bonds, citing the State’s challenge of “structural budget imbalance exacerbated by rapidly growing pension and OPEB (Other Post-Employment Benefits) costs.” Within the last few weeks, Fitch and Standard & Poor’s have each again downgraded New Jersey’s general obligation bonds. This has the potential to cost the State millions of dollars going forward in higher interest costs.

Status Report of the New Jersey Pension and Health Benefit Study Commission
Summary of Recent New Jersey Rating Actions

<table>
<thead>
<tr>
<th>Rating Agency</th>
<th>Date</th>
<th>Prior Rating</th>
<th>New Rating</th>
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</thead>
<tbody>
<tr>
<td>Standard &amp; Poor’s</td>
<td>4/9/2014</td>
<td>AA-</td>
<td>A+</td>
</tr>
<tr>
<td>Fitch</td>
<td>5/1/2014</td>
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<tr>
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<td>Fitch</td>
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</tr>
<tr>
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<td>9/10/2014</td>
<td>A+</td>
<td>A</td>
</tr>
</tbody>
</table>

Persistent Pension Underfunding

The State pension funds reported a $37 billion unfunded liability as of the end of FY 2013, the last year for which data is available. What this means is the State had on hand $37 billion less than it needed to cover the present value of: 1) the cost of providing pension benefits to current retirees and 2) the pension benefits earned through that date by current employees. Looking at the $37 billion gap another way, the plans’ combined “funded ratio,” the ratio of their $44 billion in assets to the $81 billion present value of the plans’ current obligations, was 54%. It should be noted that this is an average, as the funded ratios of the individual plans vary.

In quantifying the amount of the unfunded liability, the Commission notes that the State is required to report its unfunded pension liability in a format specified by and in accordance with the standards of the Government Accounting Standards Board (“GASB”). These standards, however, reflect actuarial methodologies which can cause reported assets and liabilities to differ significantly from how they would be reported in the private sector. As noted in the “Risks” section below, going forward, revised GASB standards will likely require lower reported values of assets. Similarly, the new standards may require use of lower expected rates of return/discount rates, which will generally increase reported liabilities.

There are many different ways to measure the same underlying unfunded liability. If the market values of assets were used, for example, the unfunded liability as of the end of FY 2013 would have been $42 billion. Similarly, the $37 billion figure reflects a 7.9% expected rate of return set by the State Treasurer. While this figure is within the range currently used by other states, the actuaries for the State’s plans have questioned its use going forward. Use of a lower expected rate of return would tend to increase the plans’ unfunded liabilities because the plans’ assets would be assumed to earn less income in future years. Given the uncertainty surrounding these factors, the best that can be said is that the State’s unfunded pension liability at the end of FY 2013 was likely at least $37 billion.

By any measure, the amount of the unfunded liability is grievous. To put funding a $37 billion gap in perspective, each of the State’s 3.2 million households would have to write a check today for approximately $12,000 to close the gap. If this payment is stretched over time, the cumulative cost per household will be even greater.

To put the severity of this crisis in a national context, NJ ranks as the 4th worst funded state in the nation with respect to funding ratio of its pensions.

Status Report of the New Jersey Pension and Health Benefit Study Commission
Bottom 5 States Based On Funded Level (Fiscal 2013)

<table>
<thead>
<tr>
<th>Bottom 5 States</th>
<th>Funded Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Illinois</td>
<td>(39%)</td>
</tr>
<tr>
<td>Kentucky</td>
<td>(48%)</td>
</tr>
<tr>
<td>Connecticut</td>
<td>(49%)</td>
</tr>
<tr>
<td>New Jersey</td>
<td>(54%)</td>
</tr>
<tr>
<td>Alaska</td>
<td>(55%)</td>
</tr>
</tbody>
</table>

New Jersey has the 4th worst funding position in the entire nation. Funding our $37 billion pension gap would require that each of the State’s 3.2 million households write a check today for $12,000.

As set forth below in Part IV, one cause of the growth of the State pension funds' unfunded liability is the drag on plan asset values caused by the 2008-09 Great Recession and the earlier 2000-02 economic downturn. Another – indeed, the initiating cause – has been elected officials making long-term commitments to provide public employee benefits that would have been affordable only under assumptions that have since proven to be unduly optimistic.

All that being said, however, the failure of the State to make required pension contributions when they have been due has made a bad situation much worse. Local governments participate in the same plans but have made more of their required payments with greater regularity, resulting in the local government share of the funds having a funded ratio of 75%, compared to the State's 54% funded ratio. Under-funding the State's share of the plans has been consistent under the stewardship of both major parties, as shown by the chart on the following page:
Actual Pension Contributions Relative to Statutory Annual Required Contributions (in Millions)\textsuperscript{12}

The 2010 and 2011 reforms, while steps toward a solution, were a political compromise, not a complete answer to the unfunded pension liability problem. The 2010 pension reforms trimmed some benefits, especially for new employees. They also established a seven-year phase-in for State employer contributions to bring them up to the full statutory ARC level. But getting the funding level to the full statutory ARC, however, is only the first step of the process. Funding would have to be maintained at that level — at whatever dollar amount it becomes based on actual future plan performance — for approximately 30 years to substantially increase the plans' funded ratio. Similarly, the 2011 pension reforms made one major change — temporarily suspending cost of living adjustments ("COLAs") — which reduced the unfunded accrued liability by $11.5 billion,\textsuperscript{13} but still left tens of billions of dollars in unfunded pension liabilities.

\textbf{High Cost State Health Programs}

The history of the two programs that provide health care coverage to New Jersey public employees and retirees (collectively, the "State Health Programs")\textsuperscript{14} has been one of a long series of benefit enhancements at State expense followed by relatively recent — and largely ineffective — efforts at cost control.

The State Health Programs provide generous benefits with little pricing incentive for employees to select anything but plans with the most comprehensive coverage and highest cost to the State. For example, as shown on the chart on page 26 comparing terms of various plans, over 80% of participants in the State Health Programs are enrolled in the NJDirect 10 and NJDirect 15 plans.\textsuperscript{15} These plans provide benefits which approach, and in some ways exceed, the "Platinum" plans available through the exchanges under the Affordable Care Act ("ACA").

The inevitable result of the absence of meaningful incentives for employees to control costs is very high costs to the State.
An additional strain on the State budget will be the 40% excise tax imposed by the ACA on high-benefit/high-cost "Cadillac" plans if they exceed a federal cost threshold. When the excise tax goes into effect in 2018, many of the most popular State plans will be classified as Cadillac plans. This will result in an estimated $58 million tax cost to the State in 2018, rising to $284 million in 2022. 17

Not only are health benefit costs high, but they also are increasing in both absolute terms and as a share of the budget. In FY 2014, those expenditures were roughly $2.8 billion after offsetting for employee contributions, or just over 8% of the budget. By 2024, unless cost containment is effected, health care benefits are projected to consume over 14% of the budget.

Projected Plan Costs for State-Paid Groups, FY2015 through FY2024 18

Without changes, health care costs are projected to consume over 14% of the State's budget by 2024.
In Search of Solutions

There is agreement, widespread and across party lines, of the need to reform public employee benefits and the State's funding of them. As former Governor Jon Corzine pointed out, "on pension and health care issues, our career employees, and the public, must recognize that current benefits are financially unsustainable. Without a dramatic increase in taxes or a draconian reduction in services, State and local government cannot meet the benefit obligations on the books."19 As Governor Christie stated in creating this Commission: "If we don't do more, and we don't do it now, we'll be forced to choose between funding what matters, or a bloated, unaffordable entitlement system we couldn't muster the will to fix once and for all."10

This shared understanding of a need for action will be helpful going forward, as there are no easy answers. On the one hand, public employees rely on these benefits for the health and financial security of their families, and the State has made a commitment to them. Furthermore, as a result of legislative changes in 2010 and 2011, employees have already made concessions with respect to reduction of benefits and increases in employee contributions. On the other hand, New Jersey already has the second-highest state and local tax burden - 12.3% of income - in the nation.11 A tax increase of this size necessary to pay for the ever-increasing cost of benefits at their existing levels is unrealistic.

Also problematic is the option of diverting a greater share of existing revenues to public employee benefits. The state budget has been virtually flat from 2008 through 2013 (declining from $33.6 billion in 2008 to $29.4 billion in 2011 before increasing to $33.0 billion in 2014).12 Any increase in funding for public employee benefits in this already tight budget would involve taking funding from schools, public safety, infrastructure, higher education and other priorities.

The purpose of this Report is not to propose solutions. It is instead to provide background and highlight issues for informed discussion. Our next report will focus on potential solutions to the State's serious pension and health benefit problems. The Commission welcomes input from stakeholders and the public at large on this issue through its website: http://www.state.nj.us/treasury/pensionandbenefitcommission.shtml.
## II. OVERVIEW: THE STATE PUBLIC EMPLOYEE PENSION AND HEALTH BENEFIT SYSTEMS

### Composition

The following table outlines, as of 2013, the State's share of the various plans and programs providing pension and health benefits to New Jersey public employees:

<table>
<thead>
<tr>
<th>Pension Plans (State Funded)</th>
<th>Acronym</th>
<th>Active Members/Subscribers</th>
<th>Retirees/Retired Subscribers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Employees' Retirement System</td>
<td>PERS</td>
<td>85,430</td>
<td>49,876</td>
</tr>
<tr>
<td>Teachers' Pension and Annuity Fund</td>
<td>TPAP</td>
<td>153,458</td>
<td>91,576</td>
</tr>
<tr>
<td>Police &amp; Firemen's Retirement System</td>
<td>PFRS</td>
<td>7,267</td>
<td>5,809</td>
</tr>
<tr>
<td>State Police Retirement System</td>
<td>SPRS</td>
<td>2,513</td>
<td>3,246</td>
</tr>
<tr>
<td>Prison Officers' Pension Fund</td>
<td>POPF</td>
<td>0</td>
<td>175</td>
</tr>
<tr>
<td>Consolidated Police &amp; Firemen's Pension Fund</td>
<td>CPPPF</td>
<td>0</td>
<td>175</td>
</tr>
<tr>
<td>Judicial Retirement System</td>
<td>JRS</td>
<td>417</td>
<td>568</td>
</tr>
<tr>
<td>Pension Plans Totals</td>
<td></td>
<td>249,085</td>
<td>151,367</td>
</tr>
</tbody>
</table>

| State Health Benefits Program-State       | SHBP    | 97,114                    | 46,651                      |
| School Employees' Health Benefits Program | SEHBP   | 0                         | 99,062                      |
| Health Benefit Programs Totals            |         | 97,114                    | 145,713                     |

### Costs

The benefits provided through these plans and programs represent a significant expense, both in absolute terms and as a share of the State budget. The State is responsible for the cost of health care for active and retired State employees and retired school employees. In FY 2014, the total cost of providing this coverage was $3.1 billion, of which $253 million was reimbursed through employee contributions, for a net expense to the State of $2.8 billion.\(^{24}\)

As set forth in greater detail below, the cost of pension benefits is harder to articulate. In FY 2014, the State actually contributed $696 million. The FY 2014 Appropriations Act had included almost $1.6 billion pursuant to 2011 legislation which called for payment of 3/7ths of the full statutory ARC. The cost of funding the statutory ARC in full would have been $3.7 billion.\(^{27}\)
The Pension System

Pension benefits are provided through a network of plans created between 1896 and 1973. Some of the pension funds have both state and local employees as members, with financial responsibility for the plans divided between the state and local governments. With two minor exceptions, the pension plans are all traditional defined benefit plans that pay a specified percentage of preretirement average salary upon retirement. The plans are capitalized, with funds set aside to pay benefits due in the future.

The terms of each pension plan vary, and, even within a plan, terms applicable to individual members vary based on date of hire. PERS and TPAF, the largest of the State pension plans, currently provide that for a new hire (benefits are greater for participants with earlier dates of hire), an employee retiring at age 65 with at least 10 years of service will receive a benefit amounting to 1.67% of the average of the employee’s five highest years of compensation for each year of service. The plan permits early retirement with a comparatively modest early retirement penalty, which for new employees is a benefit reduction of 3% a year for each year prior to age 65. It will eventually require employees to contribute 7.5% of annual salary to retirement funding.27 In addition to their pensions, State employees, unlike public employees in some other states, are also eligible for Social Security. The following information on State pension benefits for employees who retired in 2013 provides one snapshot of the system’s participants.

<table>
<thead>
<tr>
<th>2013 State Pension Plan New Retirees 28</th>
</tr>
</thead>
<tbody>
<tr>
<td>System</td>
</tr>
<tr>
<td>Public Employees Retirement System - State</td>
</tr>
<tr>
<td>Teachers Pension and Annuity Fund</td>
</tr>
<tr>
<td>State Police Retirement System*</td>
</tr>
<tr>
<td>Police and Fire Retirement System*</td>
</tr>
<tr>
<td>Judicial Retirement System</td>
</tr>
</tbody>
</table>

Note: *Special Retirement (35 years of service)

To fund the portion of pension benefits not covered by employee contributions, New Jersey law requires payment by the State of the statutory ARC. The statutory ARC consists of the “annual normal contribution” (the cost of the current year’s accruals for plan participants), and an “annual unfunded accrued liability contribution” intended to make up existing unfunded liabilities.29 The FY 2014 budget appropriated $1.382 billion for pension payments, 3/7ths of the full statutory ARC of $3.7 billion. As a result of Executive Order 156, the State paid $696 million, the full annual normal contribution portion of the FY 2014 statutory ARC, but did not pay any portion of the annual unfunded accrued liability contribution for that year.30

The State Health Programs

There are two State Health Programs. The State Health Benefits Program (SHBP), and the School Employees’ Health Benefits Program ("SEHBP"). Together, they cover employees and retirees of the State and over 1,100 local entities, although not all local government or education employers participate in the programs. As is the case with the pension plans, both the State and local governments divide financial responsibility for each of the two programs. Participating local governments are responsible for the health plan costs of their employees included in the SHBP. While participating local education employers are responsible for the health plan costs of active school employees in the SEHBP, the State is responsible for health plan costs for retired school employees, regardless of whether or not their former employers participate in the program.31

Combined, the State Health Programs offer more than 20 different medical plans administered by Horizon Blue Cross and Blue Shield of New Jersey and Aetna. They also offer seven dental plans as well as prescription drug coverage. The level of employee contribution and the manner in which that contribution is calculated has varied considerably over time. Currently, employees

Status Report of the New Jersey Pension and Health Benefit Study Commission
contribute a minimum of 1.5% of salary, paying a varying percentage of the premium costs based on their salary (at the lowest, 3% of premium cost for employees earning less than $25,000, rising to 35% for employees earning $110,000 or more). The programs will eventually require some level of contribution from retirees based on date of hire and years of service.12
III. PENSIONS

Providing for the retirement of State employees in a way that is both financially sustainable and within taxpayers’ means has for decades proven to be an intractable problem. In part this is due to the volatility inherent in defined benefit plans like the State’s. A plan’s primary liabilities (the benefits paid to employees) are designed to grow over the employees’ working careers, while the value of plan assets – particularly those invested in equities – will go up and down. The need to ensure the plan stays adequately funded during the inevitable periods when liabilities are going up while asset values are going down is a risk which must be addressed in proper management of a defined benefit plan.

Although it is possible to buffer a plan from changes in asset value through careful plan design or specially-tailored investment strategies, attaining this level of certainty can require being more modest when defining plan benefits and making and honoring commitments to fund the plan at a higher level. To operate such a plan successfully it is necessary for its stakeholders to remember in the flush years that pension surpluses may be temporary. There needs to be sufficient discipline to retain surpluses from good years as insurance against future bad years. The temptation must be resisted to use surpluses as an excuse for “contribution holidays” or as a justification for expanding benefits that cannot easily be paid for once markets have reversed and the surpluses have disappeared. Failure to follow these prescriptions set the State on an unsustainable course over a decade ago.

Adding to the technical difficulty of the problem is a lack of shared perspective. Career public employees build a lifetime of financial assumptions around the availability of these retirement benefits, and understandably view any change to them as a threat to their families’ security. The emotional impact of this issue leads to it having a symbolic and political force even beyond its considerable fiscal impact, which makes it particularly difficult for public employee representatives to make concessions on pensions. The broader tax-paying public, however, does not look at the issue from this perspective, particularly when they themselves may have to make do without pensions. Instead, the public as a whole experiences the financial burden of paying for the pension programs in the form of higher taxes and/or lower levels of State services. These conflicting perspectives create opportunities for elected officials to have it both ways. They avoid short-term pain by supporting public employee constituents when approving benefits, and taxpayers as a whole when adopting budgets, simply “kicking the can down the road” with respect to long-term financial commitments.

Magnitude of the Problem

The unfunded liability of the State plans reflects a long-term disconnect between the willingness to provide public employees with benefits and the willingness to pay for them. The consequences of this disconnect have now come home to roost.

Elected officials supported public employee constituents when approving benefits and taxpayers when adopting budgets. The consequences of this disconnect have finally come home to roost.
Pension Fund Actuarial Liabilities and Assets as of July 1, 2013 per GASB 25 and 27 (in Millions) 33

<table>
<thead>
<tr>
<th>Pension Plan</th>
<th>Actuarial Value of Assets</th>
<th>Actuarial Accrued Liability Active Portion</th>
<th>Actuarial Accrued Liability Retiree Portion</th>
<th>Total Actuarial Accrued Liability</th>
<th>Unfunded Actuarial Accrued Liability</th>
<th>Funded Ratio</th>
<th>Market Value of Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>State</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>PERS</td>
<td>$9,191.8</td>
<td>$9,700.3</td>
<td>$11,293.7</td>
<td>$19,994.0</td>
<td>$10,802.2</td>
<td>46.0%</td>
<td>$8,639.6</td>
</tr>
<tr>
<td>TPAF</td>
<td>30,606.0</td>
<td>19,562.0</td>
<td>34,085.5</td>
<td>53,645.5</td>
<td>23,039.5</td>
<td>57.1%</td>
<td>26,859.6</td>
</tr>
<tr>
<td>PFRS</td>
<td>2,033.7</td>
<td>1,541.1</td>
<td>2,647.4</td>
<td>4,188.5</td>
<td>2,154.8</td>
<td>48.6%</td>
<td>1,096.2</td>
</tr>
<tr>
<td>CP&amp;FFP</td>
<td>5.6</td>
<td>6.1</td>
<td>6.1</td>
<td>0.5</td>
<td>91.5%</td>
<td>5.8</td>
<td></td>
</tr>
<tr>
<td>SPRS</td>
<td>1,946.6</td>
<td>836.0</td>
<td>2,034.6</td>
<td>2,870.6</td>
<td>924.0</td>
<td>67.8%</td>
<td>1,832.9</td>
</tr>
<tr>
<td>JRS</td>
<td>258.5</td>
<td>184.4</td>
<td>436.0</td>
<td>620.4</td>
<td>361.9</td>
<td>41.7%</td>
<td>244.3</td>
</tr>
<tr>
<td>POPF</td>
<td>0.2</td>
<td>4.7</td>
<td>4.7</td>
<td>(3.5)</td>
<td>172.1%</td>
<td>9.0</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$44,050.4</td>
<td>$38,823.0</td>
<td>$50,506.0</td>
<td>$81,329.8</td>
<td>$37,279.4</td>
<td>54.2%</td>
<td>$39,487.4</td>
</tr>
</tbody>
</table>

| Local        |                           |                                          |                                             |                                  |                                      |             |                        |
| PERS         | $19,975.2                 | $11,230.0                                | $14,775.8                                   | $27,005.8                       | $7,030.6                            | 74.0%       | $18,120.8              |
| PFRS         | 22,097.0                  | 17,716.9                                 | 11,094.8                                    | 20,811.7                        | 7,614.7                             | 76.7%       | 20,734.8               |
| Total        | $42,072.2                 | $28,946.9                                | $25,870.6                                   | $47,817.5                       | $14,645.3                           | 75.4%       | $38,855.6              |

Keeping the existing unfunded liability from growing depends on plan assets earning a sufficient return on investment. The illustration below projects that if the market generates a 7.9% annual rate of return, the statutory ARC would level out at $5 billion for the foreseeable future. If the annual rate of return slips to 4.9%, the statutory ARC necessary to compensate for the lower rate of return would steadily grow to over $8 billion. In this illustration, only in the scenario projecting a 10.9% rate of return does the State’s required contribution finally begin to decline. It should be noted that, to simplify the illustration, the projection assumes the full statutory ARC will be paid each year, an assumption discussed further in the "Risks" section below. It also assumes that the discount rate used to determine the present value of liabilities would remain constant at 7.9%, when in actual practice this rate would be adjusted periodically to reflect market performance.
Under any likely investment return scenario, the State would need to fund $4-$6 billion annually for at least the next 20 years to close the funding gap for pensions at their current level.

How Did We Get Here?

As the table below indicates, largely due to the extremely high investment returns of the late 1990s, at the turn of the century the funded ratio of the plans based on actuarial values approached or exceeded 100%, even during the 2000-02 economic downturn. However, the apparent resiliency of the plans during that downturn is misleading. The actuarial asset values are rolling multi-year averages. For some time after the flush years of high returns, those averages continued to reflect high actuarial asset values for those years even though the market value of the assets was declining. Statutory changes also increased the expected rate of return from 7% to 8.75% and modified the actuarial funding method to allocate more costs to future years, thereby reducing the apparent value of the liabilities. This further reinforced the misperception that the plans were safely and permanently in surplus.

The reported asset values and statutory changes enabled the State, in full compliance with the standards then in place, to discontinue making contributions to the funds. While there were clear warnings then that this could lead to huge fiscal problems in the future, at the time it permitted hundreds of millions of dollars to be diverted to other purposes ranging from education to tax relief. Compounding the problem, during the years when the pension plans were apparently well-funded (but actually lapsing into deficits), the Legislature enacted a series of benefit enhancements, including a retroactive 9% increase in TPAF and PERS pensions in 2001, which increased State pension liabilities by $4.2 billion.35
### Historical Funding Status

<table>
<thead>
<tr>
<th></th>
<th>Actuarial Value of Assets</th>
<th>Actuarial Accrued Liability</th>
<th>Unfunded Accrued Actuarial Liability</th>
<th>GABS Ratio %</th>
<th>Market Value of Assets</th>
<th>Unfunded Market Value Liability</th>
</tr>
</thead>
<tbody>
<tr>
<td>FY 1997</td>
<td>31,948</td>
<td>30,717</td>
<td>1,221</td>
<td>104.9%</td>
<td>32,922</td>
<td>2,205</td>
</tr>
<tr>
<td>FY 1998</td>
<td>35,513</td>
<td>33,769</td>
<td>1,745</td>
<td>105.2%</td>
<td>41,540</td>
<td>7,772</td>
</tr>
<tr>
<td>FY 1999</td>
<td>40,076</td>
<td>36,752</td>
<td>3,326</td>
<td>109.0%</td>
<td>47,537</td>
<td>10,704</td>
</tr>
<tr>
<td>FY 2000</td>
<td>44,023</td>
<td>39,534</td>
<td>4,489</td>
<td>111.4%</td>
<td>51,612</td>
<td>12,078</td>
</tr>
<tr>
<td>FY 2001</td>
<td>50,732</td>
<td>46,552</td>
<td>4,181</td>
<td>109.0%</td>
<td>45,279</td>
<td>(1,273)</td>
</tr>
<tr>
<td>FY 2002</td>
<td>50,531</td>
<td>50,130</td>
<td>401</td>
<td>109.8%</td>
<td>39,305</td>
<td>(10,825)</td>
</tr>
<tr>
<td>FY 2003</td>
<td>49,674</td>
<td>53,914</td>
<td>(6,320)</td>
<td>92.1%</td>
<td>38,340</td>
<td>(15,574)</td>
</tr>
<tr>
<td>FY 2004</td>
<td>49,574</td>
<td>58,018</td>
<td>(9,444)</td>
<td>85.4%</td>
<td>41,144</td>
<td>(16,664)</td>
</tr>
<tr>
<td>FY 2005</td>
<td>49,755</td>
<td>62,797</td>
<td>(13,041)</td>
<td>79.2%</td>
<td>42,910</td>
<td>(19,878)</td>
</tr>
<tr>
<td>FY 2006</td>
<td>50,659</td>
<td>67,266</td>
<td>(16,607)</td>
<td>75.3%</td>
<td>45,780</td>
<td>(21,466)</td>
</tr>
<tr>
<td>FY 2007</td>
<td>52,433</td>
<td>71,656</td>
<td>(19,222)</td>
<td>73.2%</td>
<td>50,720</td>
<td>(29,936)</td>
</tr>
<tr>
<td>FY 2008</td>
<td>51,218</td>
<td>75,763</td>
<td>(23,045)</td>
<td>69.6%</td>
<td>47,009</td>
<td>(28,763)</td>
</tr>
<tr>
<td>FY 2009</td>
<td>50,230</td>
<td>80,926</td>
<td>(30,727)</td>
<td>62.9%</td>
<td>35,540</td>
<td>(44,416)</td>
</tr>
<tr>
<td>FY 2010</td>
<td>48,079</td>
<td>73,714</td>
<td>(25,635)</td>
<td>65.2%</td>
<td>37,766</td>
<td>(35,948)</td>
</tr>
<tr>
<td>FY 2011</td>
<td>46,698</td>
<td>76,806</td>
<td>(30,108)</td>
<td>60.8%</td>
<td>40,795</td>
<td>(36,010)</td>
</tr>
<tr>
<td>FY 2012</td>
<td>45,064</td>
<td>79,434</td>
<td>(34,370)</td>
<td>55.7%</td>
<td>38,271</td>
<td>(41,165)</td>
</tr>
<tr>
<td>FY 2013</td>
<td>44,050</td>
<td>81,330</td>
<td>(37,280)</td>
<td>54.2%</td>
<td>39,487</td>
<td>(41,842)</td>
</tr>
</tbody>
</table>

Just as the boom period of the late 1990s came to an end, the Legislature spent the “rainy day” fund built up during those years by increasing benefits by $4.2 billion and returning to a pattern of contribution holidays.

Increasing benefits while essentially discontinuing State contributions ultimately resulted in a rapid increase in unfunded liabilities. This increase accelerated even more dramatically as a result of the 2008-09 Great Recession, when not only did rates of return fall short of their expected levels, but substantial loss of principal also occurred. Unfunded liabilities increased at precisely the same time when, due to the economic downturn, the State faced revenue shortfalls. These lower revenues made it difficult to allocate the necessary funds to make up the growing pension shortfalls, only worsening the situation.

The reality is that we arrived at our present position by following a bipartisan course guided by Governors of both parties, as well as by a Legislature controlled by Republicans from 1995 through 2001 and by Democrats from 2004 to the present, with two years of a Democratic Assembly and an equally divided Senate in between. Public sector employees who benefited from and in many cases paid for the enhanced benefits were in agreement, as, apparently, were the voters, given incumbents’ re-election rates. Developing a common understanding of what happened and why, without allocating fault, is necessary to permit stakeholders to better discuss and evaluate potential solutions. What follows is a brief discussion of certain factors which may have had a role in creating the problem and/or might play a role in forming possible solutions.

1. **Form of Plan**

The State plans, like most public pension plans, are defined benefit plans. As set forth above, if not managed prudently, such plans can quickly slide into deficit if their risks are not properly managed and rigorous funding is not maintained. The defined contribution plans more popular in the private sector do not face this problem, as their obligations - by definition - are always equal to the sum of the participants’ account balances. However, In a broader sense, both defined benefit and defined contribution...
plans face the risk that assets will be insufficient to provide adequate retirement benefits. What differs between the two designs is who bears the immediate risk of this happening.

In a defined benefit plan the risks are borne primarily by the plan sponsor and felt, in a public sector plan, by the taxpayers who will be asked to make up any unfunded liabilities. In a defined contribution plan, the risks are borne primarily by individuals, and manifest themselves in the form of retirees outliving their retirement assets. This in turn can result in significant direct and indirect costs to family members and/or the public.

Different plan designs can work better for different workforces. In the private sector, as workforces have become more mobile and management has become increasingly unwilling to accept large, hard-to-manage long-term risks, the defined benefit plan has fallen into disfavor. Of private sector workers participating in employer-sponsored retirement programs in 2011, only 7% participated exclusively in a defined benefit plan, compared to 69% who participated in defined contribution plans only (the remaining 24% participated in programs with some combination of the two). In the public sector, where a more stable workforce places less of a premium on benefit portability and the government can take a more long-term view of risks, defined benefit plans remain more common. Boston College’s Center for Retirement Research reported that in 2012, 89% of state and local employees nationally enrolled in defined benefit plans, compared to only 2% in defined contribution plans, with the remainder in cash balance plans or “hybrid” plans that combine elements of defined benefit and defined contribution plans.

In recent years as plans have run into difficulties, however, many public employers, like private sector employers, have also become concerned about the large, hard-to-manage long-term risks of traditional pension plans. Whether the risk is due to the form of the plan or the stewardship exercised over it, there is a trend in public pension reform efforts to utilize hybrid plans as a way of fine-tuning the allocation of risk among stakeholders. As set forth in the discussion beginning on page 21, this approach can take myriad forms, and involves supplementing and/or replacing defined benefit plans with hybrid plans, defined contribution plans or both, and doing so on a mandatory or elective basis.

2. Recent State Pension Reform Initiatives

Recent reforms have brought the New Jersey pension program more in line with market norms, at least with respect to new employees. The following table summarizes key changes made in the terms of the two largest plans, PERS and TPAF, which together cover over 240,000 of the 250,000 current public employees for which the State has financial responsibility. These changes all decrease costs, and in total have reduced the State’s unfunded liability by approximately $11.5 billion.
Changes in terms of PERS and TPAF Pensions as a Result of Recent Legislative Reforms

<table>
<thead>
<tr>
<th>Provision</th>
<th>Pre-2010</th>
<th>Post 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Normal Retirement Age</td>
<td>Age 62</td>
<td>Age 65</td>
</tr>
<tr>
<td>Early Retirement</td>
<td>25 years</td>
<td>30 years</td>
</tr>
<tr>
<td>Early Retirement Reduction</td>
<td>1%/yr.</td>
<td>3%/yr.</td>
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<tr>
<td>Cost of Living Adjustment</td>
<td>Yes</td>
<td>Suspended</td>
</tr>
<tr>
<td>Employee Contributions</td>
<td>5.5%</td>
<td>Phasing into 7.5%</td>
</tr>
<tr>
<td>Vesting Period</td>
<td>10 years</td>
<td>10 years</td>
</tr>
<tr>
<td>Period for Average Salary</td>
<td>Highest 3 years</td>
<td>Highest 5 years</td>
</tr>
<tr>
<td>Formula Multiplier</td>
<td>1.818% (1/55)</td>
<td>1.67% (1/60)</td>
</tr>
</tbody>
</table>

Recent reforms made significant changes to the pension programs going forward but the unfunded liability was only reduced by ~25% because most changes had limited immediate impact on the majority of current employees.

With these and other reforms some steps toward pension reform have already been taken. One conspicuous holdover from pre-reform years, however, is the minimal per-year penalty for early retirement. A newly-hired State employee who retires five years early, at age 60, would have his or her State pension benefit cut only 3% a year, or 15%. In contrast, under Social Security, for a person born after 1960, retiring five years early – at 62 instead of 67 – would result in a 30% reduction in benefit. Early retirement has a multiplier effect on both pension and health benefit costs.

One of the reasons the reforms described above have had little impact on the unfunded liability is that many of them do not apply to all current employees. Efforts to use changes in plan structure to reduce unfunded liabilities in the near term resemble trying to use a very small tail to wag a very large dog. Illustrating this point, virtually all of the $11.5 billion in savings in pension costs effected by Chapter 78 are due to the one reform with the greatest reach beyond new employees – the temporary suspension of COLA payments. This change, of course, was almost immediately challenged in court following the enactment of Chapter 78, and remains on appeal.

3. Effect of Deferred State Contributions

While high benefit levels are one driver of unfunded liabilities, the lack of State contributions is a critical contributing factor. Put simply, if the State cannot find the economic means and discipline to consistently fund its pension obligations, the system will fail. The funding decisions over the last twenty years are telling examples of bipartisan contribution to fiscal distress.
Observers that Republicans and Democrats and both elected branches of State government are equal opportunity offenders in under-funding the pension is simply a statement of fact, but the reality is more complicated than a series of isolated decisions. Each Governor and Legislature has inherited the legacy of decisions made by their predecessors. These decisions have generally limited the available remedies while increasing their cost. Subsequent administrations have been left to support expensive benefit obligations after money that should have been set aside to pay for them was spent on other things. Not only is the principal of the contributions which should have been made missing, the investment returns these contributions would have earned have also been lost.

4. Role of Investment Decisions
A question which has been raised is whether better decisions in how the plans’ assets were invested could have avoided the unfunded liability. As seen in the graph below, while the specific time period selected has a significant impact on performance relative to expected returns, for most time periods, the overall difference between actual and expected returns is relatively small. Due to the magnifying effect of compounding, however, even differences between expected and actual returns that average out over time can have a large influence on asset values. Not only are the anticipated gains lost but the principal available to generate future income is also reduced. For example, a 20% loss on a $100 account reduces the account balance to $80. It would then take a 25% gain to move the account balance back to $100. In other words, it takes a 25% increase to merely break even after a 20% loss.

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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Statutory Annual Required Contributions</td>
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<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
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<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
</tr>
<tr>
<td>Actual</td>
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<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
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<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
</tr>
<tr>
<td>ARC Variance</td>
<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
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<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
<td>0.7</td>
</tr>
</tbody>
</table>

* Projected

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Actual and Expected Investment Return by Fiscal Year

Another relevant comparison of how New Jersey's funds fared compared to other public funds during this time period reveals that the funds performed roughly in line with peers but delivered that level of performance with less risk in the portfolio.

NJ Pension Investment Performance Relative to Other Large Public Plans as of 12/31/2013

New Jersey's investment performance generally has been in line with other large pension plans.

Finally, a few words of history may be worth many bar graphs. Part of the reason New Jersey's investment performance was so high in the late 1990s was that the State's plans had a relatively high exposure to the public equity market. When the 2000-02 downturn occurred, returns decreased accordingly. At the end of FY 2001, when the State's funds had a 63% allocation to public equities, the equities portfolio lagged the S&P 500 Index by 3.3%, losing 16.1% while the S&P 500 Index lost 12.8%, for an overall loss of 9.8%. As a result of this experience, in subsequent years New Jersey's plans followed a more conservative allocation than many peers, with somewhat less exposure to stocks and to alternative assets. This served the State plans very well in the downturn of 2008. In FY 2008, New Jersey lost only 2.6% while the S&P 500 Index lost 13.1%. In FY 2009 (which included the worst part of calendar year 2008), the State plans lost 15.5% while the S&P 500 Index lost 26.2%.
Potential Reforms

Any solution to the employee benefit funding crisis will likely involve tough choices among options that one or more groups of stakeholders may find unpleasant. The menu of options include re-allocating existing revenue from other priorities to pay for benefits, generating new revenue with additional taxes, generating new revenue from other sources such as new gambling activities or asset sales, generating new revenue from increased employee contributions, and/or reducing pension costs, or other employee benefit costs, to free up money for pension funding. Given the tightness of the State’s budget, the already high level of taxes, and the legal and political impediments to reducing benefits, there is likely no one magic bullet that will make all the problems disappear.

This is not to say, however, that progress cannot be made. Many jurisdictions have been confronted with significant unfunded pension liabilities and found ways to accomplish meaningful reform.

- One example is the federal government’s move to a hybrid defined benefits/defined contribution plan. In 1986 the newly- created Federal Employees Retirement System (FERS) for the first time enrolled federal workers in the Social Security system (a step New Jersey has already taken) to reduce retirement reliance on pensions. It then replaced its full defined benefit pension with a smaller basic annuity, supplemented by a thrift savings plan – essentially, a defined contribution plan. This reform, which had bipartisan support, reduced costs while shielding employees from the full risks of a defined contribution plan.45

- The State of Utah also opted to transition to a hybrid plan when its pension plan threatened to violate state law debt limits. The Utah hybrid plan offers employees a choice of participating in a defined contribution plan in which the State would contribute 10%-12% of employee compensation, or a defined benefit plan in which the State would contribute 10% of employee compensation – but participating employees would have to commit to contributing any additional funds required to make the annual required contribution necessary to keep the plan funded. Since a higher level of benefits requires a higher ARC contribution, this approach creates an incentive for employees to limit benefits.46 The City of Atlanta has also adopted a similar approach.47

- In 2013, Kentucky lawmakers passed comprehensive pension reform legislation with a number of different elements. It created a new pension plan for anyone hired after January 1, 2014, required that future COLAs be paid for before they are given, and included a plan that commits the Legislature to full funding of pension promises in future years. An accompanying bill raises additional revenue to help pay down past unfunded pension liability. The pension plan for new hires is a "cash balance" design which provides defined-contribution-like notional accounts but with defined-benefit guarantees. The State credits employees’ accounts with a specified percentage of their pay each year and employee contributions are added to the cash balance accounts. This design reduces the risk of under-funding over the long-term by crediting interest on accounts based on the five-year average return on trust assets. Employees making contributions to the plan receive a 4% annual return on accounts plus 75% of excess returns (based on the 5-year average returns).48

- In Baltimore, the city began offering a defined contribution option to employees. It also ended a practice in which retirees received the excess of investment earnings over a certain percentage instead of the plan retaining those earnings as a reserve against sub-par years. This practice was replaced with a more modest COLA provision available to some older retirees. This reform recently survived a federal constitutional challenge, but remains subject to state law breach of contract claims.49

- The State of Rhode Island, confronted with an unfunded liability problem, responded with a variety of reforms. It excluded certain employees from the existing defined benefit plans in favor of a hybrid plan, and offered incentives for employees not required to participate in the hybrid plan to voluntarily do so. It suspended almost all COLA payments and increased the retirement age of most employees not already eligible to retire.50
IV. HEALTH BENEFITS

Magnitude of the Problem

In FY 2014, it cost the State $2.3 billion to meet its obligations for the health care benefits of its own active employees and retirees and their dependents who are members of the SHBP, and for school retirees and their dependents who are members of the SEHBP. The breakdown of costs for the State’s share of this expense is as follows:

<table>
<thead>
<tr>
<th>FY 2014 (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Active Employees</td>
</tr>
<tr>
<td>Retirees</td>
</tr>
<tr>
<td>Active Employee Contribution</td>
</tr>
<tr>
<td>Total Net Cost</td>
</tr>
</tbody>
</table>

Employee health care costs are already 8% of the State’s annual budget and are projected to exceed $6 billion by 2024.

These expenses (including the ACA excise tax starting in 2018) are expected to more than double and exceed $6 billion by 2024, consuming an ever-increasing share of State revenues.

Projected Plan Costs for State-Paid Groups, FY2015 through FY2024

Retiree health expense is a particular area of concern, as this cost is borne by the State for an indefinite period. Moreover, the cost of retirement health care is not funded at the time the employee works, but when the expense is incurred after retirement—meaning future taxpayers will pay for the retirement health benefits of current employees. As set forth above, this future debt, while not due now, represents a $53 billion liability. Heightening concerns that these costs will be a burden on the next generation, the ratio of retirees—who contribute less to their health care costs— to active employees has been increasing. The State’s total cost of providing coverage to retirees now exceeds the cost of providing coverage to active employees, and is increasing at an even faster rate.
Total State Cost of Active Employee and State and School Retiree Health Coverage

By 2021, $1.60 will be spent on retiree medical benefits for every dollar spent on active member medical benefits.

How We Got Here

Prior to 1961, public employees had the option of purchasing, at their own expense, health care coverage through New Jersey Blue Cross/Blue Shield. In 1961, the SHBP was created to provide, at State expense, individual coverage for State employees through Blue Cross/Blue Shield and Prudential. School employees were also initially included in the SHBP, which was later expanded to include retirees and local employees and provide coverage to dependents. In 2008, the SEHBP was spun off from the SHBP to provide coverage for school employees and retirees and their dependents.

At that time, employees paid either 25% of premium cost as a health benefit plan contribution for the Traditional Plan (a non-network based Indemnity plan), 5% of the premium cost of an HMO, or no premium contribution at all for the NJ Plus network-based Point of Service option. In 2007, the State employee contribution provisions changed to require a contribution of 1.5% of salary regardless of benefit plan or level of dependent coverage selected, an approach that eliminated any meaningful financial incentive for employees to select a less expensive plan.

In parallel with the expansion of coverage available to employees, medical coverage to retirees has also expanded. As of 1972, health benefits coverage was extended to State retirees and their dependents. In 1987, the Legislature extended this post-retirement medical (PRM) coverage to school retirees. In 1997, the obligation to make some contribution for PRM was added to the terms of retirement for State employees and some local employees. Depending on their year of retirement, years of service and former employer (school retirees receive full reimbursement), retirees are also reimbursed for their Medicare Part B premiums in full (currently $104.90/month) or up to a capped amount (currently $46.10/month). Some retirees are reimbursed by the State for the income-based surcharge imposed by Medicare on high income individuals. All told, this is an annual $162 million expense.

While recent years have seen a host of efforts to reduce the cost of the State Health Programs, the success of these efforts has been mixed. The alternative Medicare Retiree prescription program offered in 2012 has been a success that has saved $150 million a year. However, as the plans are structured, there is in general not enough of a difference in cost to the employee to make electing a lower-cost plan worthwhile. For example, in 2014, for an employee earning $60,000, there is only a $44 difference in monthly cost.
to the employee between NJ DIRECT15 and NJ DIRECT2035 - a plan which over the course of a year would cost the State thousands of dollars less. 58

Similarly, to date, there has been minimal enrollment in the NJWELL program. 59 It remains to be seen whether the relatively modest rewards ($100 gift cards and possible reduction of the participating employers' insurance premiums) are of sufficient magnitude and personal relevance to make participation worthwhile to individuals.

The High Cost of the State Health Programs

The costs of the State Health Programs are far above average by any measure, as shown by this comparison of national costs, and percentage of costs paid by the employer to those of the State Health Programs.

Employer/Employee Health Care Cost Breakdown (Active Employees) 60

According to Pew Charitable Trust data, only two States had higher average costs than New Jersey.

Other data point to the same conclusion. For example, a study of public health care plans conducted as part of the Pew Charitable Trust Report found that the average per-employer per-month premium for coverage of employees and dependents was $959. The cost for NJ was $1,334, or more than 39% higher than the average. Based on the report, only two States - Alaska and New Hampshire - had higher average costs than New Jersey. 61

The reasons for this are varied. Some of the increase in costs over time is due to the general rise in medical care costs nationally. Some of the difference in State and national costs is driven by the generally high cost of obtaining medical care in New Jersey. A large part of the high and increasing costs of the State Health Programs, however, appears to be due to the extensive benefits and relatively low cost to employees of the plans most frequently selected by State Health Program enrollees. A fourth driver of cost increases - the excise tax on Cadillac plans under the ACA, is looming on the horizon.
1. Benefit and Enrollment Patterns of State Health Programs

The tendency of plan members to select the benefit options with the highest cost to the State has become a hallmark of the State Health Programs. While this tendency predates the 2011 creation of the Plan Design Committees, they have had little success altering it. The Committees are composed of an equal number of labor and employer representatives who frequently deadlock. This predisposition to inertia has inhibited changes in plan terms and pricing that would alter enrollment patterns and make the programs more efficient and cost-effective. For example, nationally, 17% of enrollees in public and private health plans elect high-deductible plan options. But among the State Health Programs, the participation rate in high-deductible plans is only 0.06% (only 137 of 242,827 State active and retiree and education retiree enrollees have selected the HD4000 or HD1500 high-deductible options).42

Well over 80% of the participants in the State Health Programs are enrolled in plans that exceed the benefits of the “Gold” plan available through the ACA exchanges.

Similarly, as set forth on the chart on the following page, of 242,827 State active employees and State and education retirees participating in the State Health Programs, 209,506 are enrolled in plans that exceed the benefits of the “Gold” plan available through the federal health care exchange under the ACA, and approach or exceed terms of the “Platinum” ACA option.43
2. Relative Expense of Health Care in New Jersey

While factors intrinsic to the benefit offerings and enrollment patterns of the State Health Programs have contributed to their high and increasing costs, it should be noted that even a well-designed program in New Jersey is likely to have higher than average costs due to the higher cost of care in the State. This is illustrated by the relative cost of certain common procedures in New Jersey compared to the cost of those procedures in other geographic areas, a problem whose causes transcend the scope of this Commission's charge.

Procedure Cost by Geography

<table>
<thead>
<tr>
<th></th>
<th>NJ</th>
<th>Northeast</th>
<th>South</th>
<th>Midwest</th>
<th>West</th>
</tr>
</thead>
<tbody>
<tr>
<td>Back Procedure</td>
<td>10,482</td>
<td>9,556</td>
<td>10,482</td>
<td>17,016</td>
<td></td>
</tr>
<tr>
<td>Hip Arthroplasty</td>
<td>11,085</td>
<td>9,117</td>
<td>11,085</td>
<td>12,119</td>
<td></td>
</tr>
<tr>
<td>Spinal Cord Procedure</td>
<td>11,851</td>
<td>11,380</td>
<td>11,851</td>
<td>14,831</td>
<td>16,708</td>
</tr>
</tbody>
</table>

Some common medical procedures cost the State more than twice the cost of the same procedure elsewhere.

3. Increases in Cost of Medical Care

As the following chart indicates, it is not a question of if medical costs will increase, but how quickly this will happen. The lowest indicator of medical cost inflation, the national Medical CPI index, shows annual medical costs increasing at a rate varying between 2% and 4%. Medical costs tend to increase faster than the Medical CPI on account of new procedures and medications with higher costs, the aging of the insured population (especially as the baby boomers retire), and increased use of services as rising medical costs decrease the efficacy of fixed deductibles and co-pays as cost-control devices. The fact that costs will be increasing due to factors beyond the State’s control underscores the importance of taking action on drivers of costs the State can control.

The fact that costs will also be increasing due to factors beyond the State’s control underscores the importance of taking action on drivers of costs the State can control.
Medical Cost Inflation Over 10 Years

4. Impact of the ACA Excise Tax

Also as noted above, starting in 2018, a 46% ACA excise tax will be imposed on the aggregate value of plans in excess of an indexed threshold. The thresholds are currently set at $10,200 for individual coverage and $27,500 for family coverage in 2018, with slightly higher thresholds for early retirees and high-risk occupations like police and fire. Due to the nature of the plans offered by the State Health Programs, and because New Jersey is a relatively high-cost state (the ACA excise tax is not adjusted for geographic differences within the United States), some plans offered by the State Health Programs will be subject to the excise tax as soon as it goes into effect, and virtually all current plans will be subject to the excise tax by 2022. It is projected that the ACA will increase the State Health Programs’ costs by an additional $58 million in FY 2018, rising to $284 million by 2022.67

Potential Reforms

While recommending specific reforms is outside the scope of this Report, as a general matter, the plan structure and enrollment patterns of the State Health Programs need to evolve to reflect the realities of the 21st century. Among the approaches others have used to bring the costs of their public employee health plans more in line with those of the private sector are:68

<table>
<thead>
<tr>
<th>Reference Based Pricing</th>
<th>High Deductible Plans</th>
<th>Tobacco Surcharge</th>
<th>Spousal Surcharge</th>
<th>Dependent Eligibility Audit</th>
<th>Value Based Insurance Design</th>
<th>Onsite Clinics</th>
</tr>
</thead>
<tbody>
<tr>
<td>CA</td>
<td>GA</td>
<td>AL</td>
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<tr>
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<td>WI</td>
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<td>WI</td>
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</table>

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V. PENSION AND BENEFIT COSTS IN THE CONTEXT OF THE OVERALL BUDGET

As background for future discussion of how to reconcile potential employee benefit funding remedies with existing budget constraints, the major categories of expenditures and revenues are displayed below.

**FY 2015 Appropriations Act Details (% of Total Spending)**

<table>
<thead>
<tr>
<th>Category</th>
<th>$ (Billion)</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Children and Families</td>
<td>1.1</td>
<td>3.4%</td>
</tr>
<tr>
<td>Corrections</td>
<td>1.1</td>
<td>2.7%</td>
</tr>
<tr>
<td>Education</td>
<td>10.6</td>
<td>30.8%</td>
</tr>
<tr>
<td>Human Services</td>
<td>6.6</td>
<td>19.3%</td>
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<tr>
<td>Higher Education</td>
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<td>4.0%</td>
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<tr>
<td>Transportation</td>
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<td>4.2%</td>
</tr>
<tr>
<td>Treasury</td>
<td>1.5</td>
<td>4.7%</td>
</tr>
<tr>
<td>Other*</td>
<td>2.4</td>
<td>7.3%</td>
</tr>
<tr>
<td>Interdepartmental and General Obligation Debt Service</td>
<td>1.9</td>
<td>5.6%</td>
</tr>
<tr>
<td>Total Pensions and Health Benefits (State, local education)</td>
<td>4.0</td>
<td>12.4%</td>
</tr>
<tr>
<td>Legislature/Judiciary</td>
<td>0.8</td>
<td>2.4%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$ 32.5</strong></td>
<td><strong>100.0%</strong></td>
</tr>
</tbody>
</table>

Notes: *Combines all other Executive Branch agencies (e.g., Agriculture, Banking and Insurance, etc.).

This list of line items, taken from the FY 2015 budget, suggests the hard choices which would have to be made regarding possible services to cut in order to allocate more of existing revenues to public employee health benefits. At the risk of being simplistic, without additional revenues, funding an expense like the $1.56 billion unfunded liability payment originally scheduled for FY 2015 would, within the FY 2015 budget, require something as drastic as cutting the Corrections, Higher Education and Transportation budgets in half. Funding the full statutory ARC would be even more difficult.
Even if the voters can be persuaded to provide some additional revenue, there is a limit to the extent the problem can be solved by simply directing more money to it. Currently, employee benefits are approximately 10% of the budget. This percentage would have to be raised to 20% to fund the current annual gap. Raising the equivalent of an additional 10% of existing revenues by increasing the amount of revenue raised through one or more of these sources would be painful and difficult, particularly if taxpayers react in ways that decrease the activities to be taxed.

Moreover, even finding an additional 10% of revenue would not solve the problem for long. Pension and health costs are growing faster than the projected 4% growth of State revenues. The budget projections in Appendix 3 estimate that by 2024, the share of employees' benefits would increase further to almost 25% of the State budget. This would require even more additional revenue to close the widened gap.
VI. RISKS

The success of any solution to the benefit funding crisis will be affected by a number of risks:

- **Non-payment.** Two decades of history underscore the possibility that the State, through legislative and/or executive action, may not fund its employee benefit obligations. Experience has shown that unfunded obligations, if not corrected, have the potential to grow so large they cannot be made up. In addition to the financial risk, the lack of trust resulting from successive government failures to make payments will make any long-term solution more difficult to achieve.

- **Investment under-performance.** The current expected rate of return on State pension funds (which serves as the discount rate for reducing future liabilities to present value) is 7.9%. In its recent construction bond disclosures, the State noted that the independent actuary for all the State pension funds other than TPAF found that 7.9% was at the high end of an acceptable expected rate of return. The independent actuary for TPAF considered 7.9% to be outside a reasonable range, and recommended use of a reduced expected rate of return. Elsewhere, the disclosure notes that the new GASB Standards may require the use of a discount rate lower than the 7.9% rate currently used. Whatever expected rate of return is used, there continues to be the risk future returns may fall short of that rate, resulting in growing unfunded liabilities and plan contribution requirements. The higher the expected rate of return, the greater the exposure to this risk.

- **Health care cost inflation.** Health care costs are projected to increase at an annual rate of 7.5%, and aggregate cost increases will be even higher due to the ACA excise tax. These costs are growing at a rate faster than the expected rate of growth of State revenues. If actual costs increase in accordance with these trends, maintaining the same level of benefits will consume an ever-increasing share of State revenues.

- **Interest rates.** One of the costs competing with employee benefits for scarce State resources is debt service. At present, interest rates are extraordinarily low. Any increase in those rates -- and it is likely a question of when rather than if the increase will occur -- will increase debt service demands that will place considerably more tension on an already tight budget.

- **Legal.** The current $37 billion unfunded pension liability reflects a reduction of $11.5 billion due to the Chapter 78 reforms — mostly due to the temporary suspension of COLAs to current and future retirees. If that suspension is overturned as a result of ongoing litigation, it will make a deep hole even deeper, and have a significant long-term impact on funding requirements of the plans. There is also currently pending a lawsuit that challenges the State’s decision not to remit the entirety of the statutory ARC for FY 2014 and FY 2015.
VII. A CALL TO ACTION

This Report has examined the nature, scope and causes of New Jersey's public employee pension and health benefits problem. This issue is particularly important to State employees and retirees and their families, but also significantly affects all New Jersey citizens as taxpayers and as beneficiaries of State services. There is no choice: New Jersey must make its public employee pension and health benefits program affordable and sustainable.

The Commission's final Report will recommend possible solutions to this problem for consideration by the Governor and the Legislature. In the coming weeks we will be considering proposed solutions, and we will continue to review actions taken by other states and municipalities to solve similar problems. We will study reports of policy experts and consider all suggestions and comments from citizens and groups interested in this problem. We welcome all ideas, which can be submitted to us through the Commission's website: http://www.state.nj.us/ treasury/pensionsandbenefitscommission.shtml

This problem is dire and will only become much worse if meaningful steps are not taken quickly.
APPENDIX 1 — BIOGRAPHIES OF COMMISSION MEMBERS, STAFF AND COUNSEL

Commission Members

Thomas J. Healey, CFA, Partner, Healey Development LLC
Tom Healey is coordinating the work of the Study Commission. He is a Senior Fellow at Harvard University’s John F. Kennedy School of Government, where he taught a course in Financial Institutions and Markets. In 2010 he received the Mossavar-Rahmani Center for Business and Government’s Distinguished Service Award. He is a retired partner of Goldman, Sachs & Co. While at Goldman Sachs, he created the Pension Services group, the first of its kind in financial services, servicing the top 100 leading Pension and Endowment Clients globally. Tom also chaired Goldman Sachs’ own Pension Plan and served as CIO of the Central States Teamsters Pension Plan. Prior to joining Goldman Sachs, he served as Assistant Secretary of the U.S. Treasury for Domestic Finance under President Ronald Reagan. Tom is a chartered financial analyst and graduated from Georgetown University and Harvard Business School.

Margaret S. Berger, FSA, EA, FCA, Principal, Mercer
Margaret Berger is a consulting actuary and Principal in Mercer’s Retirement Practice. She manages actuarial project teams and provides actuarial consulting on defined benefit plans, nonqualified plans and retiree medical and life insurance plans. Based in Princeton, Margaret is also a member of Mercer’s Actuarial Resource Network, which helps consultants solve complex technical actuarial problems and recommends and implements pension valuation standards throughout the firm. Margaret has 24 years of experience consulting in the area of retirement benefits. She has helped clients on a wide range of assignments, such as performing annual actuarial valuations of pension and postretirement welfare plans including the review and development of actuarial assumptions and methods, preparing financial statement footnote disclosure information, designing/redesigning retirement benefits. Margaret is a member of the American Academy of Actuaries Pension Committee and the Actuarial Standards Board Pension Committee. Margaret received a BA in Mathematics from Yale University. She is an Enrolled Actuary, a Fellow of the Society of Actuaries and a Fellow of the Conference of Consulting Actuaries.

Tom Byrne, Managing Member, Byrne Asset Management LLC
Tom Byrne is managing member of Byrne Asset Management LLC in Princeton, an investment advisory firm that manages $150 million for a variety of clients. In the 1990s and before, he worked at two major New York law firms and later in the securities industry in Manhattan. He has served in a number of volunteer and non-profit capacities as well. He is currently vice chairman of the New Jersey State Investment Council. He is also a trustee and treasurer of The Fund for New Jersey. Tom served as chairman of the New Jersey Democratic State Committee in 1994-97. He also served on the staff of The Presidential Task Force on Market Mechanisms, which reported to President Reagan on the causes of the 1987 stock market crash. He is a 1976 graduate of Princeton University’s Woodrow Wilson School and has served on its graduate advisory board. He has a law degree from Fordham University.

Raymond G. Chambers
Ray Chambers is a philanthropist and humanitarian who has directed most of his efforts towards helping children. He is the United Nations Special Envoy for Financing the Health Millennium Development Goals. Ray was the Chairman of Wesray Capital and began his career as a CPA with Price Waterhouse Coopers. He is the founding Chairman of the Points of Light Foundation and co-founder, with Colin Powell, of America’s Promise — Alliance for Youth. He also co-founded the National Mentoring Partnership and the Millennium Promise Alliance. Chambers is the Co-founder of Malaria No More. He is the Founding Chairman of the New Jersey Performing Arts Center.

Leonard W. Davis, CFO, Revelation Holdings, Inc.
Len has organized and managed private equity, technology, and natural resource companies. He has been the principal financial manager in a private equity company and has been the Chief Financial Officer to the lead investor of a natural resource company active in metals and energy. His experience spans a wide range of businesses including private equity, investment banking, leveraged buyout, and M&A. His management experience includes due diligence on acquisition investments, acquisition and exit strategy, and investment analysis. Before entering private equity, Len was a CPA in public practice at Price Waterhouse, LLP ("PW") in New York (now PriceWaterhouseCoopers) in their

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Personal Financial Service Group. He provided tax planning and general business advice to wealthy individuals and their companies while at PW. Prior to joining PW, he was employed in the Private Banking Group of J.P. Morgan Services, Inc. He received his B.S. in Accounting from Spring Garden College.

Carl A. Hess, FSA, CERA, Managing Director, Towers Watson
Carl Hess has served as Managing Director, The Americas of Towers Watson since February 1, 2014, and is a member of the firm’s Executive Committee. Prior to that, he served as the Managing Director of Towers Watson’s investment business since January 1, 2010. Before that, he worked in a variety of roles over 20 years at Watson Wyatt, lastly as Global Practice Director of Watson Wyatt’s Investment business. Carl is a fellow of the Society of Actuaries and the Conference of Consulting Actuaries, and a Chartered Enterprise Risk Analyst. He has a B.A. cum laude in Logic and Language from Yale University, and is a director of HLC Holdings and its subsidiaries and affiliates.

Rihan Kra, Ph.D., FSA, EA, CERA, Rihan E. Kra Actuarial Services
Dr. Rihan Kra is an independent and highly respected consulting actuary. Previously, he was a Senior Partner and Chief Actuary—Retirement of Mercer. He specializes in analyzing the economic and accounting implications of financing strategies and vehicles for employee and executive benefits. For over 17 years, he chaired Mercer’s Actuarial Resource Network, a committee of the society’s few technical actuaries throughout the United States. Ethan is a Fellow of the Society of Actuaries, a Member of the American Academy of Actuaries, a Fellow of the Conference of Consulting Actuaries, a Member of ASPPA, an Enrolled Actuary and a Chartered Enterprise Risk Analyst. He has served on the American Academy of Actuaries Board of Directors, as its Vice President, Pensions and Chair of its Pension Practice Council. He is a Summa Cum Laude graduate of Yale University, where he earned his B.A. in Mathematics and was elected to Phi Beta Kappa. He holds M.A. and Ph.D. degrees in Mathematics from Yale University, where he was both a Woodrow Wilson Fellow and a National Science Fellow.

Kenneth F. Kunzman, Partner, Connell Foley
Kenneth F. Kunzman was Chairman of the Connell Foley Executive Committee from 1995 to 2002. He has been a partner in the firm since 1968 and has been responsible for a variety of areas of law. Ken is a graduate of The College of the Holy Cross and Fordham University Law School. He is Chairman of the Board of the Bonner Foundation, former Chairman of the District Ethics Committee, Trustee Emeritus of Caldwell College, former Trustee of St. Peter’s Prep, and Co-Chairman Emeritus of the Seton Hall University Pirate Blue Fund. He served as Captain, US Air Force from 1962-1965. Ken has been Co-Counsel since 1978 of the Pension and Welfare Funds for Locals 472 and 172 Heavy and General Laborers Fund of New Jersey. He has been elected to the Super Lawyers and Best Lawyers of America since inception.

Lawrence J. Sher, Partner, October Three
Lawrence J. Sher is a partner, consulting actuary, and member of the Senior Leadership Team at October Three, which is a full service, actuarial, consulting and technology firm that is a leading force behind the reemergence of defined benefit plans across the country. With over 35 years of consulting experience, Larry served as chief actuary at other leading consulting firms, has frequently advised government officials on retirement issues and has been a speaker at numerous professional and industry conferences. As a nationally recognized expert on cash balance and other hybrid pension plans, he is a highly sought-after consultant and advisor to retirement plan sponsors. In addition, he provides critical support as a consulting and testifying expert in disputes related to cash balance plans and other retirement programs. Larry is a Fellow of the Society of Actuaries (FSA), a Fellow of the Conference of Consulting Actuaries (FCA), a member of the American Academy of Actuaries (MAAA), and an Enrolled Actuary (EA) under ERISA. He has been a Board Member and Vice-Chair of the Actuarial Standard Board, a Board Member of the American Academy of Actuaries and the Conference of Consulting Actuaries, and he was recently President of the Conference of Consulting Actuaries.

Raj Tatta, Retired Senior Partner, PricewaterhouseCoopers LLP
During his 30-year career at PricewaterhouseCoopers LLP, Raj Tatta served some of the firm’s largest global clients and managed different businesses, including serving as the partner-in-charge of Europe for the U.S. Tax practice. Raj took early retirement from PwC to volunteer for organizations focused on the mentoring and development of inner city youth, like the Big Brothers Big Sisters and the All Stars Project. Raj has also been involved in global health issues: he was part of the senior leadership team charged with restructuring the Geneva-based Global Fund to Fight AIDS,
Tuberculosis and Malaria; and more recently, assisted the UN Secretary General’s Special Envoy for Financing the Health Millennium Development Goals. Raj serves on a few corporate and volunteer boards, including as President of the Park Avenue Club in Horseshoe Park, which benefits 10 local charities. Raj holds CPA and MBA qualifications.

Executive Director

Matthew W. King
Matthew W. King is a private investor. Previously, he was a Director at Kohlberg, Kravis, Roberts and Co, as well as KKR Capstone, where he focused on building new lines of business for KKR, due diligence on new investments and improving the operating performance of KKR’s portfolio companies. He previously served on the Board of Directors for Sealy Corporation and Corporate Capital Trust. He received a B.S. summa cum laude from North Carolina State University in Mechanical Engineering and Economics.

Commission Counsel

George H. Kendall, Partner, Drinker Biddle & Reath LLP
George H. Kendall is a partner in Drinker Biddle & Reath LLP’s Florham Park, New Jersey office. George serves as the Vice Chair of Drinker Biddle’s Health Care Practice Group. He represents hospitals, hospital systems, home health agencies, physician groups, pharmaceutical, medical device and medical equipment companies in a broad range of transactional and regulatory matters. George received his A.B. from Franklin & Marshall College and his J.D. from the Villanova University School of Law. He has been recognized by Chambers USA as one of the top health care lawyers in New Jersey.

Kenneth J. Wilbur, Partner, Drinker Biddle & Reath LLP
Kenneth J. Wilbur is a partner at Drinker Biddle & Reath LLP’s Florham Park, New Jersey office. He represents a variety of life science and real estate clients in commercial, products liability and appellate litigation. He received a B.A. summa cum laude from Lehigh University and a J.D. cum laude from the University of Pennsylvania School of Law, and clerked for the Hon. Alan B. Handler, Associate Justice, Supreme Court of New Jersey.

Thomas F. Campion, Partner, Drinker Biddle & Reath LLP
Thomas F. Campion is a partner at Drinker Biddle & Reath LLP’s Florham Park, New Jersey office. He specializes full-time in litigation at the trial and appellate level for life science companies and other businesses and professions. He received his A.B. magna cum laude from Fordham University and his LL.B. from Cornell Law School.
APPENDIX 2 — GLOSSARY

Actuarial Accrued Liability (AAL)
The present value of future benefits attributable to service rendered to date. That would include the present value of all future pensions payable to current retirees, beneficiaries and vested terminations, plus the present value of a portion of the projected benefits for active employees.

Actuarial Value of Assets (AVA)
The actuarial value of a plan’s assets. This amount spreads recognition of investment gains and losses in accordance with an adopted asset valuation method.

Annual Normal Contribution
The portion of the ARC reflecting the cost of the benefits accrued during the current year by plan participants.

Annual (or Actuarial) Required Contribution (ARC)
The ARC equals the amount that would need to be paid during the current fiscal year to fund benefits earned in that year (the normal cost) plus a specified portion of any unfunded liability from past years.

Annual Unfunded Accrued Liability Contribution
The portion of the ARC reflecting the cost of funding a specified portion of any unfunded liability from past years.

Defined Benefit Plan (DB)
For defined benefit (DB) plans, benefits are generally expressed and paid as life annuities beginning at retirement, based on one or more specified benefit formulas. These formulas generally incorporate years of service, salary and a multiplier factor. Specific benefit formulas vary among plans, and often within plans dependent on an employee's start date and/or employee classification (public, safety, general, management, etc.). Some more recent defined benefit plans express benefits in terms of a current lump sum value (similar to a defined contribution plan) rather than a retirement age annuity, although these plans too must offer life annuities. Defined benefit annuity payments can either be constant for the life of the payment, adjusted annually for cost of living, or adjusted occasionally for cost of living increases as seen fit by the overseeing party. The plan sponsor is responsible for funding this liability no matter what returns it achieves on its investments.

Fiscal Year (FY)
The State budgets on a fiscal, not calendar year basis. FY 2014 began on July 1, 2013, and ended on June 30, 2014.

Defined Contribution Plan (DC)
For defined contribution (DC) plans, the plan sponsor makes contributions into individual employee accounts under the plan and sometimes employees also make contributions to their accounts. A common example of a DC plan is a 401(k) found in the private sector. The actual benefit received by participants is subject to market returns on the plan’s assets. The sponsor has no liability to make up for investment losses.
Funded Ratio
The percentage of the Actuarial Accrued Liability that is currently funded through the Actuarial Value of Assets. This is calculated by dividing AVA by the AAL. A ratio of less than 100% indicates that the plan has an unfunded liability. If over 100%, the plan has a surplus.

Market Value Method of Asset Valuation
Under the market value method, plans recognize the full amount of actual gains or losses at the end of each fiscal year.

Plan Year (PY)
The State Health Programs operate on a Plan Year which coincides with the calendar year.

Smoothing Method of Asset Valuation
Smoothing spreads changes in reported asset values due to deviations between expected returns and actual results over a period of years. Assuming a rolling five-year smoothing period, 20% of any variation between expected and actual results for a given year would be incorporated into the AVA in the valuation year.

Unfunded Actuarial Accrued Liability
The AAL minus the AVA – unfunded if positive and surplus if negative.
<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>Lost</th>
<th>Unemployed</th>
<th>Disability</th>
<th>Retirement</th>
<th>Other</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2023</td>
<td>1000</td>
<td>50</td>
<td>300</td>
<td>200</td>
<td>400</td>
<td>100</td>
<td>1000</td>
</tr>
<tr>
<td>2024</td>
<td>1050</td>
<td>55</td>
<td>320</td>
<td>230</td>
<td>430</td>
<td>110</td>
<td>1150</td>
</tr>
<tr>
<td>2025</td>
<td>1100</td>
<td>60</td>
<td>350</td>
<td>260</td>
<td>460</td>
<td>120</td>
<td>1200</td>
</tr>
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</table>

**Notes:**
- Data includes all categories.
- Total figures cover all state revenues.
### Summary of Pension Projections ($ billions)

**Summary of Pension Projections based on varying levels of investment return on actuarial assets**

<table>
<thead>
<tr>
<th>Year</th>
<th>Actuarial Assumptions</th>
<th>Investment Return</th>
<th>Actuarial Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>2024</td>
<td>1%</td>
<td>3%</td>
<td>4%</td>
</tr>
<tr>
<td>2025</td>
<td>2%</td>
<td>3%</td>
<td>4%</td>
</tr>
<tr>
<td>2026</td>
<td>3%</td>
<td>3%</td>
<td>4%</td>
</tr>
</tbody>
</table>

**Notes:**
- Actuarial Assumptions:
  - 1%: Low
  - 2%: Medium
  - 3%: High
- Investment Return:
  - 3%: Low
  - 4%: Medium
  - 5%: High
- Actuarial Return:
  - 4%: Low
  - 5%: Medium
  - 6%: High
END NOTES

1 See Appendix 2 Glossary for definition of fiscal year.

2 As further defined in the Appendix 2 Glossary, ARC refers to the “actuarial” (the term generally used in pension literature) or “annual” (the term used in New Jersey statutes defining this obligation) required contribution. ARC is the amount that would need to be paid during the current fiscal year to fund benefits earned in that year, plus a portion of any unfunded liability from past years. The “statutory ARC” is the payment amount as defined by formula set forth in New Jersey statutes.

3 Treasury Data. New Jersey pre-funds pensions to, in a broad sense, fund the liabilities at the time the underlying benefits are earned. Virtually all states use a similar approach. This creates “generational fairness” – future generations do not have to pay for liabilities they did not create. New Jersey, like most other states and private corporations, does not pre-fund retiree health care liabilities, although this future expense is reported as a liability. This has the effect of transferring the expense of funding one generation’s retiree health benefits to the following generation. Theoretically these policies are inconsistent, but it is how the practice has evolved.


5 Treasury Data compiling actuarial plan asset and liability data from Milliman, Inc. (actuaries to TPAF) and Buck Consultants (actuaries to all other State pension funds).

6 Id. A plan’s “funded ratio” is the percentage of the present value of the funds’ liabilities (pension payments to current and future retirees and associated expenses) covered by the present value of the assets of the fund (comprising of employer and employee contributions and interest on the funds’ assets). A plan with a funded ratio of 100% has enough funds on hand to pay 100% of its anticipated liabilities for benefits attributable to benefits rendered to date - assuming its investments earn the expected rate of return. To the extent a plan does not have enough funds to cover its anticipated liabilities, it has an “unfunded liability.” See Appendix 2 Glossary.


8 Division of Pensions and Benefits internal document. The actuarial values reported by the State in accord with Government Accounting Standards Board (“GASB”) standards, are “smoothed” to average values over a number of years. This reduces the impact of year-by-year value fluctuations on pension funding.


10 Data available at: http://quickfacts.census.gov/qfd/states/34000.html

11 Treasury Data compiling actuarial plan asset and liability data from Milliman, Inc. (actuaries to TPAF) and Buck Consultants (actuaries to all other State pension funds).
12 Division of Pensions and Benefits internal document.

13 Treasury Data.

14 The two programs are the State Health Benefits Program ("SHBP"), and the School Employees Health Benefits Program ("SEHBP").

15 Aon Data. The NJDirect10 plan is only available to current education retirees and some State retirees.


17 Aon Data.

18 Treasury Data.


22 Treasury Data.

23 Treasury Data. The apparent disparity between there being approximately 400,000 active and retiree members of the pension system but only 240,000 active and retiree participants in the health plan is that certain active local employees, such as teachers, have the option to participate in a locally-sponsored health plan.

24 Treasury Data.

25 Treasury Data.

26 The Alternate Benefit Program is a defined contribution system for higher education employees, and the Defined Contribution Retirement Program is a defined contribution system for elected and appointed officials and employees subject to a pensionable salary cap for wages above the cap.

27 L. 2011, c. 78.
TREASURY DATA.

See Glossary, Appendix 2.

TREASURY DATA.


TREASURY DATA. For TPAF, market value does not include $136.1 million in CGIPF assets. For liabilities, TPAF includes NCGL and CGIPF.

TREASURY DATA compiling actuarial plan asset and liability data from Milliman, Inc. (actuaries to TPAF) and Buck Consultants (actuaries to all other State pension funds).

L. 2001, c. 133.

Division of Pensions and Benefits internal document.


L. 2010 c. 1; L. 2011 c. 78.


Division of Pensions and Benefits internal document.

TREASURY DATA.

Wilshire Data. Any inconsistency in the return rate figures depicted here and in the previous graph is due to the previous depicting fiscal year data and this graph depicting calendar year data.

Data available at: http://www.state.nj.us/treasury/pensions/anmprts-archive.shtml


Ronald Snell, State Defined Contribution and Hybrid Pension Plans, National Conference of State Legislatures, at 5, 8 (2010).


51 Treasury Data.

52 Treasury Data.

53 Treasury Data.

54 Treasury Data.

55 Treasury Data (historical); Aon Data (projections).


57 Treasury Data.

58 Aon Data.

59 Aon Data.

60 See note 17.


64 Aon Data.

65 Aon Data.

66 SHBP/SEHBP represents changes in year-over-year claim cost per employee for the total group, normalized for plan changes. Aon Trends include historical as well as projected health care cost trends. Medical CPI is based on changes in the All Urban Consumers Medical CPI.
67 Aon Data.

68 Aon Data.

69 Treasury Data.
