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Analysis

H.B. 337 - Rep. Blasdel

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Staff Recommendation

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H.B. 337 would make the following changes to the alternative retirement plans (ARP) for higher education employees:

- Make all full-time employees of a public institution of higher education eligible to elect an ARP.

Current law allows only full-time faculty or unclassified administrative staff members who are not receiving a benefit from a state retirement system to elect to participate in the ARP.

- Give all eligible employees employed at a public institution of higher education on the effective date of the bill (including those who were previously eligible to select the ARP but chose not to) 120 days after the bill's effective date to elect to participate in the ARP. All eligible employees hired after the effective date of the bill would have 120 days from the date of employment to elect to participate in the ARP.

When the ARP was first established, it was available to new hires and current members with less than five years of total service credit.

- Allow an employee who is participating in an ARP and changes providers to transfer all or part of the account balance to the new provider.

Current law requires the entire balance to be transferred to the new provider.

- Change the employer contribution rate to an ARP to be equal to the percentage the employer would have contributed on behalf of that employee to the state retirement system that would otherwise cover the employee minus the percentage contributed by the employer as a supplemental contribution to the retirement system.

Current law allows the board of trustees of each public institution to determine the employer contribution rate to an ARP.

Staff Comments - The bill would expand the current ARP by allowing all full-time employees of a public institution of higher education, including reemployed retirants and employees with more than five years of service credit, to elect the ARP. In all cases of doubt, the board of trustees of the public institution of higher education shall determine whether the person is an eligible employee, and its decision is final.

Current employees would have 120 days after the bill's effective date to elect to participate in the ARP. The election becomes effective as of the date on which the employee's election to

participate in the ARP becomes irrevocable (i.e., at the expiration of the 120 day election period). New hires would have 120 days after the start of employment to elect the ARP. An employee who, after the effective date of the bill terminates employment at one public institution of higher education and is later employed by another public institution of higher education may elect to participate, within 120 days of employment, in an ARP at that institution. The employee's election becomes effective on the starting day of employment.

All elections become irrevocable after the 120-day election period has expired and continues to be irrevocable for the duration of the electing employee's employment by that public institution. An employee who fails to make an election within the 120-day period is deemed to have elected to participate in the appropriate state retirement system. An employee who elects to participate in an ARP is barred from claiming or purchasing service credit under any state retirement system for the period of employment while the election is in effect.

An eligible employee who elects to participate in an ARP must submit the election in writing to the employer's designated officer. The officer shall file a certified copy of the election within ten days of the election taking effect to the state retirement system that would have otherwise covered the employee.

The alternative retirement plan for academic or administrative employees of public institutions of higher education was first established in 1997 by Am. Sub. H.B. 586 (eff. 3-31-97). H.B. 586 defined academic or administrative employees as full-time faculty or administrative staff of a public institution of higher education who serve in an unclassified civil service position and are not receiving any benefits from PERS, STRS, or SERS. It was available to current academic or administrative employees as of the effective date of the bill who had less than five years of service credit and to all academic or administrative employees hired after the effective date of H.B. 586. Under the original provisions of H.B. 586, when an employee elected an ARP, the amount transferred by the retirement system for current employees as of the effective date of the ARP was limited to employee and employer contributions beginning on the date the employee became eligible to elect the ARP and ending on the day before contributions to the ARP began, minus the supplemental contribution rate.

Under H.B. 337, when an eligible employee elects to participate in an ARP, the retirement system must transfer to the ARP provider employee and employer contributions beginning on the employee's starting date of employment and ending on the day before the day on which contributions to the ARP begin, minus the supplemental contribution rate. For newly hired employees, this would mean that the transferred amount of money would be limited to the 120 day election period at a maximum. However, for eligible employees who are employed before the effective date of the bill, it is unclear whether it would encompass the contributions made during the entire time the employee had been contributing to the retirement system or limited to the employee's employment at that particular public institution of higher education. We interpret

this section to mean the amount of contributions made to the retirement system during the entire time the employee had been contributing to the system. Under either interpretation, there is the potential for this period to be much longer than the 120 day limit for new employees.

We would recommend that participation in an ARP be limited to (1) full-time employees of a public institution of higher education hired after the effective date of H.B. 337, (2) current full-time employees of a public institution of higher education who were hired after the effective date of H.B. 586 (3-31-97), but before the effective date of H.B. 337 who have less than five years of service as of the effective date of H.B. 337, and (3) any eligible employee of a public institution of higher education who was employed by a public institution of higher education at the time H.B. 586 was enacted and who would have been eligible to participate under the provisions of H.B. 586 if it had been open to all full time employees (i.e., all full-time employees with less than five years of service as of April 1, 1998 for members of PERS and SERS and as of the thirtieth day of June immediately preceding the date an ARP is adopted at the public institution where the member is employed for members of STRS). This change would be consistent with the eligibility requirements for the systems' defined contribution plans, which limits participation to newly hired employees and employees with less than five years of service prior to the establishment of the plan.¹ It would also treat those individuals who were employed when H.B. 586 was enacted, but were excluded from the bill, the same as the faculty and administrative employees who were given the option to participate in an ARP originally.

If the ARP were limited as recommended above, the amount transferred by the retirement systems for current members with less than five years of service as of the effective date of the bill would be limited in the same manner as the transfer in H.B. 586 (i.e., employee and employer contributions beginning on the date the employee became eligible to elect the ARP and ending on the day before contributions to the ARP began, minus the supplemental contribution rate), thereby limiting the amount. For members who would have otherwise been eligible to participate in an ARP under H.B. 586, the amount of the transfer would equal the amount that would have been contributed had the member elected to participate in an ARP pursuant to H.B. 586. The member may keep any contributions that are not transferred with the system or upon application by the member transfer the refund amount to the ARP. The refund amount under STRS equals employee contributions plus interest, along with a 50% match from employer contributions for members who had a least five years of service. The refund amount under PERS equals employee contributions plus interest, along with a 33% match of employer contributions for members with five but less than 10 years of service and a 67% match for members with ten or more years of

¹The STRS defined contribution plan was authorized by S.B. 190 (eff. 7-13-00) and went into effect on July 1, 2001. The PERS defined contribution plan was authorized by H.B. 628 (eff. 9-21-00) and went into effect on January 1, 2003. The SERS defined contribution plan was authorized by S.B. 270 (eff. 4-9-01), but has not gone into effect.

service. The refund amount under SERS equals the amount contributed by the employee.

H.B. 337 would also include state university law enforcement officers as employees eligible to elect an ARP. These employees are currently in the law enforcement division of PERS (PERS-LE). The very nature of law enforcement employment calls into question the appropriateness of extending an alternative retirement plan to these public employees. The extensive disability and survivor coverage provided under the defined benefit plans offered by the retirement systems immediately upon employment is of particular value to these public employees due to the hazardous nature of their employment. No provision for disability or survivor benefits is made under the ARP. The survivors of members of PERS-LE who are killed in the line of duty or die from injuries sustained in the line of duty also qualify for benefits under the Ohio Public Safety Officers Death Benefit Fund. The Death Benefit Fund provides survivor benefits equal to the full monthly salary of the deceased member, plus any salary increases that would have been granted had the member not died, minus any survivor benefits paid by the state retirement system. Again, no provision for these benefits is made under the ARP. OP&F and HPRS do not offer defined contribution plans and members of PERS-LE are currently excluded from participation in PERS' defined contribution plan for these reasons. *Therefore, we would further recommend that H.B. 337 be amended to exclude all state university law enforcement officers from participation in an ARP.*

When the ARP was first established, employers who had employees participating in an ARP were required to contribute six percent of the employee's salary to the applicable state retirement system to mitigate any negative financial impact on the system's funding resulting from the establishment of an ARP. There were three reasons why the supplemental rate is needed. First, existing unfunded actuarial liabilities of the systems must be amortized and each system relies on contributions on behalf of all employees in the groups currently covered by the retirement systems to amortize these liabilities. Second, employees who are most likely to join the ARP are those who expect to receive less benefits from the retirement system than from the ARP and vice versa, which serves to increase system costs. Third, university and college employees eligible to join an ARP generally receive compensation higher than the average compensation provided to other members of the retirement systems. Because health insurance does not vary in proportion to earnings, if employees with higher than average earnings transfer to an ARP, employer contributions to finance health insurance will decrease disproportionately.

The ORSC is required to have an actuarial study completed every three years that determines any necessary adjustments in the supplemental contribution rate. Any benefit increases enacted after March 31, 1997 (the effective date of H.B. 586) is excluded from the the retirement system's unfunded pension liabilities for purposes of determining the duration of the rate. In addition, the employer supplemental contribution rate to the ARP is limited to the supplemental contribution rate PERS, STRS, and SERS establish for their defined contribution plans (H.B. 94, eff. 9-5-01). The systems are required to calculate the supplemental contribution rate for their

defined contribution plans annually. The most recent ORSC report on the supplemental contribution rate for higher education employers was completed July 1, 2002. Although Milliman found that the the STRS supplemental contribution rate to the ARP should be 4.20%, it is limited to 3.5% because that is the rate STRS has established for its defined contribution plan. As of January 1, 1999 the supplemental contribution rate payable to PERS was reduced to 0.0% because the December 31, 1998 Valuations for Active and Inactive Members and for Retired Lives for PERS indicated that the unfunded actuarial accrued liability was fully amortized as of that date. (The supplemental contribution rate for the PERS defined contribution plan is also set at 0.0%.) As of July 1, 2000 the supplemental contribution rate payable to SERS was reduced to 0.0% because the June 30, 2000 Annual Basic Benefits Actuarial Valuation for SERS indicated that the unfunded actuarial accrued liability was fully amortized as of that date. (SERS does not currently have a defined contribution plan.) *We would recommend that the supplemental contribution rate for the ARP be set at the same rate established by the systems for their defined contribution plans and that any change in the supplemental contribution rate for the ARP rate would be effective on the same day the rate change for the defined contribution plan takes effect. This would be consistent with the requirement that the employee and employer contribution rates for members of the ARP are tied to the contribution rates established for members of the applicable retirement system.*

The current statutory language is unclear as to whether the supplemental contribution rate to the ARP resumes if the systems go from being fully funded to having an unfunded liability. This issue has been raised by the ORSC actuary, Milliman USA, in their review of H.B. 337 and in prior reports regarding the supplemental contribution rates. In their actuarial review of H.B. 337, Milliman provides two alternatives that could be used to determine the time period over which supplemental contributions would be payable. The alternatives are (1) the funding period reported in the annual actuarial valuation of the retirement system next following the establishment of the ARP; or (2) the funding period reported in the most recent annual actuarial valuation of the retirement system minus an adjustment to decrease that period to reflect benefit increases subsequent to March 31, 1997, which the supplemental contributions should not assist in financing.

According to Milliman, the first alternative would ignore actuarial gains and losses subsequent to the establishment of the ARP while the second would adjust the period during which the supplemental contribution would be payable to reflect them. The second alternative would allow the supplemental contribution to be reinstated in the event that future actuarial losses exceed any remaining unamortized unfunded actuarial pension liabilities that were created by benefit improvements allocated to retirement system members only. It would be necessary for PERS, STRS, and SERS to identify the portion of the unfunded actuarial liability attributable to benefit increases subsequent to March 31, 1997 each year in order to implement this alternative. *We would recommend that the current statutory language be clarified to state that the supplemental contribution will resume if unfunded actuarial liabilities reemerge due to actuarial losses and that*

it would be payable over a time period set as the funding period reported in the most recent annual actuarial valuation of the retirement system minus an adjustment to decrease that period to reflect benefit increases subsequent to March 31, 1997.

H.B. 337 would also require the employer contribution rate to an ARP to be equal to the percentage the employer would have contributed on behalf of that employee to the state retirement system that would otherwise cover the employee minus the percentage contributed by the employer as a supplemental contribution to the retirement system. Currently, the board of trustees of each public institution of higher education is permitted to determine the rate it contributes to an ARP. This is inconsistent with the amount employers must contribute for all other members. Current law requires employers to contribute the following amounts for employees participating in the systems' traditional defined benefit plans:

SYSTEM	EMPLOYER CONTRIBUTION RATE
PERS State	13.31%
PERS Local	13.55%
PERS Law A	16.70%
PERS Law B	16.70%
STRS	14.00%
SERS	14.00%

Employers of members who elect to participate in a system's defined contribution plan must contribute an amount equal to the percentage the employer would have contributed on behalf of that employee to the state retirement system that would otherwise cover the employee minus the percentage contributed by the employer as a supplemental contribution to the retirement system. The change in H.B. 337 is consistent with the contribution rate employers must pay to the system's defined contribution plan and treats similarly situated employees the same. It is also consistent with the employee contribution rate for members of the ARP because the employee rate is tied to the rate contributed by members of the applicable retirement system.

Additionally, we would recommend the following technical changes be made to the bill:

- *In line 70, after "3305.05" insert "or 3305.051";*
- *In line 170, after "3305.05" insert "or 3305.051";*
- *In line 179, after "3305.05" insert "or 3305.051";*
- *In line 183, after "3305.05" insert "or 3305.051";*
- *In line 187, after "3305.05" insert "or 3305.051";*

- *In line 459, delete "division (A)" insert "division (B)";*
- *In line 474 delete "division (B)" insert "division (C)";*
- *In line 482 delete "division (B)(2)(a)" insert "division (C)(2)(a)";*
- *In line 559, after "3305.05" insert "or 3305.051";*
- *In line 567, after "3305.05" insert "or 3305.051";*
- *In line 575, after "3305.05" insert "or 3305.051";*
- *In line 638, after "any" insert "eligible";*
- *In line 798, after "3305.05" insert "or 3305.051";*
- *In line 833, after "3305.05" insert "or 3305.051";*
- *In line 870, after "3305.05" insert "or 3305.051";*
- *In line 885, after "3305.05" insert "or 3305.051".*

Fiscal Impact - The ORSC actuary, Milliman USA, reviewed the actuarial analyses prepared by the PERS, STRS, and SERS actuaries. According to Milliman's review, each system used slightly different assumptions regarding which members would be likely to join an ARP and had somewhat differing understandings of exactly how to determine the total employee and employer contributions to be transferred to an ARP on behalf of members who elect to transfer. However, they generally concluded that the estimated effect of H.B. 337 would be relatively de minimus on the actuarial status of the mandated pension benefits. It should be noted that the SERS actuary estimated that the transfer of current members to an ARP due to H.B. 337 could reduce contributions available to fund discretionary health care benefits by \$2 to \$4 million per year if as many as 50% of the eligible members elected to transfer. These transfers could cut SERS resources to provide discretionary health care benefits by roughly 2%. Milliman noted that since SERS does not offer a defined contribution alternative to members, it seems reasonable to anticipate that they may have a higher percentage of their members electing to transfer to an ARP than PERS and STRS. PERS and STRS may have some members choose to remain if they are satisfied with their defined contribution option. (See attached actuarial analysis.)

ORSC Position - At the March 10, 2004 meeting of the Ohio Retirement Study Council, the Council voted to recommend that the 125th Ohio General Assembly approve H.B. 337 upon the adoption of the following amendments:

- *that participation in an ARP be limited to (1) full-time employees of a public institution of higher education hired after the effective date of H.B. 337, (2) current full-time employees of a public institution of higher education who were hired after the effective date of H.B. 586 (3-31-97), but before the effective date of H.B. 337 who have less than five years of service as of the effective date of H.B. 337, and (3) any eligible employee of a public institution of higher education who was employed by a public institution of higher education at the time H.B. 586 was enacted and who would have been eligible to participate under the provisions of H.B. 586 if it had been open to all full time employees;*

- *that H.B. 337 be amended to exclude all state university law enforcement officers from participation in an ARP;*
- *that the supplemental contribution rate for the ARP be set at the same rate established by the systems for their defined contribution plans and that any change in the supplemental contribution rate for the ARP rate would be effective on the same day the rate change for the defined contribution plan takes effect. This would be consistent with the requirement that the employee and employer contribution rates for members of the ARP are tied to the contribution rates established for members of the applicable retirement system;*
- *that the current statutory language be clarified to state that the supplemental contribution will resume if unfunded actuarial liabilities reemerge due to actuarial losses and that it would be payable over a time period set as the funding period reported in the most recent annual actuarial valuation of the retirement system minus an adjustment to decrease that period to reflect benefit increases subsequent to March 31, 1997; and*
- *that the above-mentioned technical changes be made to the bill.*