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# *Analysis*

## **H.B. 600 – Rep. Wachtmann** *(As Introduced)*

December 10, 2008

### **ORSC Position**

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H.B. 600 would make the following changes to the laws governing the Public Employees Retirement System (PERS):

- Change the purchase price for the following types of service credit:
  - Service while on Worker’s Compensation;
  - In-term salary increase for elected officials barred from receiving the increase due to Constitutional limits;
  - Prior service for elected officials;
  - Additional 35% service for elected officials and certain appointed officials;
  - Exempted service;
  - Service while on leave of absence or resignation due to pregnancy;
  - Credit for service between 1/1/1935 and date of becoming member;
  - Out-of-state, federal, or service covered under a municipal retirement system in Ohio; and
  - Service where an employee is prevented from making contributions due to illness, injury, or other reason approved by employer.
  
- Repeal the following obsolete sections of the Revised Code:
  - §145.02 – purchase of service before 8/20/1976 barred from PERS due to receipt of benefits from municipal retirement system and service before 11/21/1969 barred from PERS due to receipt of benefits from state or local police or fire pension fund or HPRS.
  - §145.292 – purchase of credit for prior employment with municipal zoo or zoological society;
  - §145.42 – purchase of credit under the United States Employment Service; and
  - §145.44 – purchase of credit under local retirement system.
  
- Eliminate the obsolete term “prior service,” which is service rendered before January 1, 1935.
  
- Limit a survivor’s right to purchase service credit after a member’s death to only those credit purchases that were initiated by the member prior to the member’s death and allows survivors of members who died prior to the effective date of the bill to purchase credit for one year after the effective date of the bill.

Current law allows survivors to purchase any type of service credit a member would have been eligible to purchase prior to death.

- The changes would be effective January 1, 2010.

**Staff Comments** – H.B. 600 would change the purchase price for a number of types of service credit. The following chart provides a listing of each type of credit, the current purchase price, and the price a member would be required to pay under H.B. 600:

<b>Type of Service</b>	<b>Current Purchase Price</b>	<b>Purchase Price Under H.B. 600</b>
Service while on Workers' Compensation (up to 3 years) (R.C. §145.2914)	No cost to member	Member pays employee contributions that would have been paid, plus interest; employer pays employer contributions that would have been paid, plus interest
In-term increase in salary for elected officials Constitutionally barred from receiving increase (R.C. §145.2915)	Employee contributions on the additional salary official would have otherwise been eligible to receive, plus interest	Member pays employee and employer contributions that would have been made
Prior service for elected officials (R.C. §145.20)	Member rate in effect at time of payment x salary for period of service, plus interest	100% of the additional liability
Additional 35% service for elected officials and certain appointed officials (R.C. §145.201)	Member rate in effect at time of payment x salary for period of service x 2	100% of the additional liability
Exempted service (R.C. §145.28)	Member salary for 12 months preceding purchase x rate established by board (currently 20%)	100% of the additional liability
Service while on leave of absence or resignation due to pregnancy (R.C. §145.291)	Member rate in effect at time of payment x salary prior to leave, plus interest	100% of the additional liability
Credit for service between 1/1/1935 and date of becoming member (R.C. §145.292)	Member rate in effect at time of payment x salary for period of service, plus interest	100% of the additional liability
Out-of-state, federal, or service covered under municipal retirement system in Ohio (R.C. §145.293)	Member contribution for first year of full-time Ohio service following termination of service to be purchased, plus interest	100% of the additional liability
Employee prevented from making contributions (R.C. §145.47(C))	Contributions that would have been paid (payment must be made within one year)	100% of the additional liability

In 2007 the ORSC asked its actuary, Milliman, Inc. to complete a report on the cost of purchasing service credit. The report, entitled *Report Regarding Service Purchases*

*Experience of the Five Ohio Retirement Systems During FY Ending 2005* was presented at the March 14, 2007 ORSC meeting. The report revealed that the retirement systems subsidized the purchase of credit in nearly every case in 2005. This was true even for service credit for which the member was required to pay the full actuarial cost. The actuarial cost of service is dependent upon the member's final average salary, years of service, and age at retirement. None of these factors are known until a member retires. Therefore, the true actuarial cost of purchasing service can be known only at retirement. This raised the public policy issue of whether a member's purchase of service credit should be subsidized by the retirement system. When a member pays less than the full cost of the additional liability created by the purchase, an unfunded liability is created. This unfunded liability must be paid for out of employer contributions.

The purchase of credit creates two types of additional liabilities: pension and health care. Although pension benefits are set by statute and become vested once a member retires, health care is discretionary and, therefore, the additional health care liability will change as changes are made to the health care plan. As Milliman noted in the report, health care liabilities created by the purchase of service could be eliminated if the purchased service did not count toward eligibility for or the amount of health care benefits. Currently, members of PERS and SERS are statutorily prohibited from using purchased out-of-state, federal, non-interrupted military, exempt, and early retirement incentive service credit from being used to qualify for health care eligibility.

Since 1989 the General Assembly has consistently been requiring members to pay more of the actuarial liability created by their purchase of service credit. In 1989, the law was amended to require STRS members to pay at least 50% of the additional actuarial liability created by the purchase (H.B. 293, eff. 9/15/89). This change applied to (1) any person establishing STRS membership for the first time on or after July 1, 1989 regardless of when the service to be purchased occurred and (2) any service that commences on or after July 1, 1989 regardless of when membership is established.

In 1991, members of PERS, STRS, and SERS were first permitted to purchase credit for school board service provided they paid the entire additional liability resulting from the purchase. They also had to agree to retire within 90 days after receiving notice from the retirement board of the additional liability resulting from the purchase (H.B. 382, eff. 6/30/91). In 1992, the law was amended to require members of OP&F who purchase credit for time they were laid off to pay the full cost of the additional liability created by the purchase (H.B. 394, eff. 9/3/92). Beginning in 1994, OP&F members who purchase out-of-state or federal service are required to pay the entire additional liability created by the purchase and they must also retire within 90 days of the purchase (H.B. 197, eff. 10/11/94).

The law was changed in 2000 to require members of PERS to pay at least 50% of the actuarial cost for military service that does not interrupt public employment (H.B. 186, eff. 3/17/00). The most recent change that required members to pay more of the additional liability for purchases occurred last session in H.B. 71 (eff. 3/3/07). That bill allowed members of PERS, STRS, SERS, and HPRS to purchase service credit for active

duty in the Ohio National Guard or armed forces reserves that consists of assembly for drill and instruction; training at encampments, maneuvers, outdoor target practice, or other exercises; and any training or duty in this state ordered by the governor if the member pays **100%** of the resulting additional actuarial liability. Because these types of service do not interrupt public employment, they are not covered by the federal Uniformed Services Employment and Reemployment Rights Act of 1994 (USERRA). USERRA requires a member whose public employment is interrupted by military service to be treated as though his or her public service was not interrupted, which means the system may require the member to pay the employee contributions that would have been made during that time period.

In response to that report, staff recommended, and the Council approved at the 9/12/2007 ORSC meeting that

1. The purchase price for all types of service should be the full actuarial liability resulting from the purchase of service credit, except as prohibited by federal law, and members should be required to retire within 90 days of purchasing service.
  - The rationale behind this change would end the current practice whereby all members of the system subsidize a member's purchase of service credit. It is also consistent with recent legislative changes that have required members to pay more of the additional actuarial liability resulting from the purchase of service credit.
2. Purchased credit should be prohibited from being counted for purposes of health care eligibility or subsidy.
  - As noted in the Milliman report, this would eliminate the additional health care liabilities created by the purchase of credit. This could be done by legislation or administrative rule.

This bill is consistent with those recommendations, however, it does not require the member to retire within 90 days of purchasing the service nor does it prohibit the purchased service from being counted for purposes of health care eligibility or subsidy. Additionally, it applies only to PERS. *Therefore, we would recommend that the bill be amended to require the member to retire within 90 days of purchasing the service and to prohibit the purchased service from being counted for purposes of health care eligibility or subsidy. We would further recommend that the bill be amended to include the comparable sections of the Revised Code governing the State Teachers Retirement System, the School Employees Retirement System, the Ohio Police & Fire Pension Fund, and the Highway Patrol Retirement System.*

**Fiscal Impact** –The PERS actuary, Gabriel, Roeder, Smith & Company, made the following observations:

1. Once an effective date is announced, it is likely that there will be a surge of people trying to complete or initiate purchases prior to the effective date. This could lead to as many as 15,000 additional applications for service purchase and possibly as much as \$100 million in unanticipated service purchase costs. Based upon the results of the December 31, 2007 valuations, each \$100 million affects the reported amortization period by about one year.

2. The effects of the proposed changes to the in-term increase in salary for elected officials are expected to be minimal.
3. The expected changes from repealing the various code sections are minimal.

**ORSC Position** –At the December 10, 2008 meeting of the Ohio Retirement Study Council, the Council voted to recommend that the 127<sup>th</sup> Ohio General Assembly approve H.B. 600 upon the adoption of the following amendments:

- An amendment that would require the member to retire within 90 days of purchasing the service and to prohibit the purchased service from being counted for purposes of health care eligibility or subsidy.
- An amendment to include the comparable sections of the Revised Code governing the State Teachers Retirement System, the School Employees Retirement System, the Ohio Police & Fire Pension Fund, and the Highway Patrol Retirement System.