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***H.B. 520 of the 131st
General Assembly***

Rep. Schuring

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Staff Recommendation

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Summary of H.B. 520

H.B. 520 makes administrative and clarifying changes to the laws governing the five state retirement systems. It makes a number of substantive changes. It also modifies the calculation used to determine the mitigating rate applying to alternative retirement plan (ARP) participants.

Staff Comments

The majority of the changes in the bill relate to administrative and clarifying changes, which are listed below as dot pots. ORSC staff recommends approval of all of the following changes as they improve the operation of the retirement systems:

Changes affecting multiple systems

- Provides survivor benefits until age 22 to the qualified child of a Public Employees Retirement System (PERS), State Teachers Retirement System (STRS), or Ohio Police and Fire Pension Fund (OP&F) member who dies before retirement regardless of whether the child is attending an institution of learning or training.
- Provides death benefits from the Ohio Public Safety Officers Death Benefit Fund until age 22 to the surviving child of a public safety officer regardless of whether the child is attending an institution of learning or training.
- Eliminates provisions under which a PERS, STRS, or School Employees Retirement System (SERS) member who earns service credit in more than one system during the same time period receives partial credit from each system in which credit is earned.
- Requires that any legal action commenced against OP&F or STRS be filed in Franklin County.¹

Public Employees Retirement System

- Requires a PERS disability benefit recipient to undergo a periodic, rather than annual, medical examination.
- Reduces to two months (from three) the time a PERS member or re-employed retirant must wait to receive a refund of the member or retirant's PERS contributions.
- Specifies that the last established beneficiary of a deceased PERS member who was also a member of STRS or SERS is the sole beneficiary in all the systems if a

¹ Note that, should H.B. 503/S.B.303 apply to the state retirement systems, this requirement would conflict with the citizen cause of action provisions of those bills.

survivor benefit may be paid under provisions coordinating PERS, STRS, and SERS benefits.

Ohio Police and Fire Pension Fund

- Establishes as conditions for return of contributions of an OP&F member who terminates active service that two months have elapsed and the member has not returned to active service during the two-month period.
- Requires a deceased member's accumulated contributions that are not claimed within seven years to be transferred to the Guarantee Fund and paid to the member's survivor or the member's or survivor's estate on application to the OP&F Board.
- Specifies that money due or to become due to an individual from OP&F is not subject to the operation of bankruptcy or insolvency laws but is subject to an order for division of marital property.
- Requires an application submitted to OP&F to be in the form and manner specified by the Fund.

State Teachers Retirement System

- Excludes from "compensation" for purposes of STRS contributions and benefits any portion of the amount paid to a teacher as a retroactive payment of earnings, damages, or back pay under a court order or settlement agreement that is excluded from compensation under continuing law.
- Revises when the STRS Board terminates payment of a disability benefit.
- Eliminates the dollar amount multiplier that may be used to calculate the pension portion of an STRS disability retirement benefit.
- Allows an STRS member to receive credit for the period as a recipient of an STRS disability benefit if the member has become a contributor to the STRS defined contribution plan and earns at least two additional years of service credit.
- Makes a recipient of an STRS allowance or benefit beginning on or after August 1, 2013, that was immediately preceded by a disability benefit that was terminated on or after that date, eligible for a cost-of-living adjustment on the date that would have been the disability benefit's next anniversary date.
- Authorizes the STRS Board to establish a plan for retirants re-employed as teachers under which the retirant's STRS contributions are invested at the retirant's direction in accordance with investment options established by the Board and, if the Board establishes a plan, requires STRS to transfer each retirant's contributions to it.
- Requires STRS to withhold or recover from the recipient of an STRS retirement or disability benefit who is employed in a position subject to CRS any amount that is to be forfeited under CRS requirements.

- Requires certain STRS members who purchase service credit for an absence or leave due to illness, injury, or professional reasons to purchase the credit by paying STRS instead of treating it as a pass through from the member's employer.
- Includes in the benefit used to calculate future cost-of-living adjustments paid a survivor of a deceased STRS member who was receiving a disability benefit any increases the member received while receiving the disability benefit.
- Eliminates the minimum survivor benefit dollar amount for qualified STRS survivors whose benefits are based on the number of qualified survivors.
- Clarifies that any return of contributions or unpaid disability benefits payable to a deceased STRS member's beneficiaries are to be paid to the beneficiaries designated by the member.

State Highway Patrol Retirement System

- Provides for designation of beneficiaries by State Highway Patrol Retirement System (SHPRS) members and retirants.
- Specifies that a surviving spouse of a deceased SHPRS member or retirant is eligible for a monthly pension based on the member's or retirant's age and service only if the member or retirant had at least 20 years of service credit.
- Clarifies that only SHPRS members who are eligible for retirement with an unreduced pension may elect to participate in the system's deferred retirement option plan (DROP).
- Changes the effective date of a member's election to participate in DROP to the first day of the first payroll period immediately following the SHPRS Board's receipt of the election (instead of the date the member files the election).
- Permits SHPRS retirants to authorize dues checkoffs on behalf of certain organizations composed of retired State Highway Patrol employees.

The bill includes the following changes of note:

- Suspends or terminates the PERS disability benefit of a recipient who *fails*, rather than *refuses*, to file required information with the PERS Board. LSC staff noted in their analysis that the change does not include an exception for an individual who is incapacitated and incapable of submitting the form.² However, ORSC staff is comfortable with the change as PERS currently has a one year suspension period during which an incapacitation issue is resolved.³

² LSC Analysis, "H.B. 520 of the 131st General Assembly, As Introduced," 11.

³ R.C. 145.362(B).

- Requires for transfer to PERS or purchase of Cincinnati Retirement System (CRS) credit in PERS that a PERS member have more PERS service credit than the amount of CRS credit to be transferred or purchased.⁴
- Requires for transfer of PERS credit to CRS that a CRS member have more CRS service credit than the amount of PERS credit to be transferred.⁵
- Eliminates provisions under which an STRS member may purchase credit for school board service only if the member is or will be eligible to retire and retires within 90 days after purchasing the credit. Note that this is not altering the cost of service credit purchases made under pension reform. The 90-day requirement is no longer necessary as all purchases must be 100% of the additional liability.⁶
- Causes certain future community (charter) school nonteaching employees to be excluded from SERS. The change removes a membership determination for individuals that do not exist due to the timing of the effective date of the charter school changes. The amendment removes a provision that had no effect as the specified individuals do not, and will not, ever exist.⁷
- Requires an SHPRS member to have at least five years of service credit to be eligible for off-duty disability retirement. SHPRS currently provides *on-duty* disability retirement immediately on employment. The other law systems require five years of employment prior to being eligible for *off-duty* disability retirement. *ORSC staff, therefore, recommends this policy change as it would standardize the off-duty disability retirement provisions between the law enforcement systems.*⁸
- Requires a disability pension to be terminated if an SHPRS disability retiree is re-employed as a law enforcement officer. *While this is a policy change, it is a logical extension of disability re-employment provisions applicable to all of the state retirement systems; therefore, ORSC staff recommends the ORSC approve this change.*⁹
- Removes the requirement that actions of the SHPRS Board be approved by a majority of the Board's members. Currently only SHPRS and SERS require a majority of members, rather than a majority of a quorum, to take action. ORSC staff is neutral on this change as there are valid arguments to be made under both voting requirements. However, as this change would make SERS the only system requiring a majority of member voting, we would advise SERS staff to consider whether their current voting requirements make sense.¹⁰

⁴ R.C. 145.2911.

⁵ R.C. 145.2912.

⁶ R.C. 3307.78.

⁷ R.C. 3309.013.

⁸ R.C. 5505.18(A).

⁹ R.C. 5505.18(F) and (G).

¹⁰ R.C. 5505.04.

H.B. 520 includes the following three provisions that ORSC staff recommends be modified or removed for further review and interested party discussion:

- Excludes employer contributions from "compensation" for purposes of STRS additional annuity payments amounts that are in excess of certain percentage increases.¹¹ ORSC staff recommends that the portion of the employer match returned to the member be tied to the withdrawal portion, as this provision appears to be closest to a withdrawal (although the comparison is not exactly the same), which is currently provided at 50%. ORSC staff agrees that the member should not receive 100% of the employer contribution (as provided in current law) as there is no other situation of full withdrawal of employer contributions in STRS law. *However, ORSC staff recommends that this provision either be pulled from H.B. 520 for further review or set to match the withdrawal rate, rather than 0%, of those employer amounts.*
- Excludes from use in determining eligibility for STRS retirement, disability, or survivor benefits, certain military service credit transferred to STRS from OP&F, SHPRS, or CRS. This non-USERRA credit is used in determining the benefit amount but not eligibility for a benefit. *This is a standardization of a policy change made in pension reform that currently applies to PERS and SERS credit transferred to STRS.¹² However, with other issues related to service credit transfers present (see below dot), ORSC staff recommends greater review of this provision with interested parties.*
- Establishes conditions for an SERS member to elect a purchase or transfer of service credit from OP&F or SHPRS to SERS and between SERS and CRS.¹³ This change would match a provision added to PERS law in S.B. 42 of the 130th General Assembly. Since the enactment of that bill, existing provisions of law result in some members with split service between the systems being unable to transfer credit. *ORSC staff recommends the transfer provision be reviewed to determine if a resolution can be made on this issue prior to replicating the provision of concern to another retirement system.*

The bill also includes the following policy changes.

Mitigating Rate

Background

¹¹ R.C. 3307.501(D).

¹² R.C. 3307.58(A).

¹³ R.C. 3309.73, 3309.731, 3309.75(B), and 3309.76(A).

In December of 2014, ORSC staff issued a report on the employer contribution rate diverted to a retirement system to mitigate the negative financial effect of the alternative retirement plan (ARP).¹⁴ That study noted that the calculation was unnecessarily opaque, inconsistent, and not in line with the directives of the General Assembly. Staff listed six considerations that could be included in developing a new formula. Subsequent to that study, Am. Sub. H.B. 64 of the 131st General Assembly froze the mitigating rate as follows but did not adjust the statutory formula:

PERS 0.77%

STRS 4.50%

SERS 6.0%

H.B. 520 proposes to eliminate the frozen rates and modify the actual formula used in determining the mitigating rate in PERS, STRS, and SERS. The intent of the proposal is to create a calculation that includes both the unpaid historical accrued unfunded liability (UAL) resulting from previous participation in ARP, plus the liabilities caused by the future loss of an employment position resulting from current ARP participation. The calculation of the bill is as follows:

- 1) Determine the “historical percentage.” This is the portion of the existing UAL attributed to ARP at the time the initial study is conducted (December 2016).¹⁵
- 2) For the initial mitigating rate study in December 2016, determine the following:
 - a) Calculate an amount necessary to amortize over a perpetual period (greater than 100 years) the historical UAL attributed to ARP plus the portion of existing UAL that is attributed to ARP, considering the compensation of those ARP participants.¹⁶
 - b) Determine a rate applying to ARP members that would amortize the amount under (a) as calculated above, over a perpetual period.
 - c) Determine the mitigating rate, which will be the greater of 1/4th of the “historical percentage” or the rate determined under (b), not to exceed 4%.
- 3) For each subsequent 5-year study after 2016, determine the following:
 - a) Calculate the same amount as under (2)(a) above, except this time determine the historical UAL by multiplying the historical percentage by the UAL of that most recent actuarial study.

¹⁴ Jeff Bernard, “Alternative Retirement Plan Mitigating Rate: Report on Rate History and Operation, as Required by Am. H.B. 483 of the 130th General Assembly” (December 11, 2014).

¹⁵ For instance, if the UAL of PERS is \$100, and \$10 of that is attributed to ARP participation, the historical percentage would be 10%.

¹⁶ By considering the compensation of those existing ARP members, the UAL attributed to ARP could be higher, if ARP participants on average earn more than a typical retirement system member, or lower, if ARP participants on average earn less than a typical retirement system member.

b) Determine a rate applying to ARP members that would amortize the amount under (a) as calculated above, over a perpetual period.

c) Determine the mitigating rate, which will be the greater of 1/4th of the "historical percentage" or the rate determined under (b), not to exceed 4%.

Expressed as a shortened and simplified formula:

1) Mitigating rate = Greater of ((Historical ARP UAL + existing ARP UAL) amortized over a perpetual period and expressed as percent of ARP payroll) or (.25%(historical percentage)), not to exceed 4%.

ORSC staff recommends the implementation of the concept of this formula. To demonstrate why this is the case, what follows is the original six suggestions made by ORSC staff to clarify the mitigating rate formula and the manner in which the proposed formula resolves that suggestion:

1) *Recognize that there is a negative financial impact on the retirement system due to ARP participation and that this effect is related to the UAL.* The proposed formula acknowledges the negative financial impact both historically and currently and ties that negative impact directly to UAL in a predictable, measurable manner.

2) *That a consistent formula be established in statute to provide clarity and consistency for employees, employers, and the retirement systems.* As a statutory formula based on an actual UAL figure present in the systems financial statements, the proposed formula will provide consistency over time and eliminate the opaqueness of the current formula.

3) *That the formula use as its central data point the most recent unfunded accrued liability rate for the relevant system.* The key data point in the proposed formula is the UAL attributed to ARP membership.

4) *That the General Assembly consider and specify the extent of the mitigation provided by ARP employers and whether there is a cap on that amount.* The formula answers this question by providing for the higher of one-fourth of the historical or current rate, not to exceed 4%.

5) *Whether the mitigation of the unfunded accrued liability owed by employers has a termination date.* The formula addresses this recommendation by recognizing both the historical and current UAL effect of ARP membership and continues this recognition into the future.

6) *Whether adjustments to the unfunded accrued liability should be made to account for benefit increases, benefit decreases, 13th check provisions (in the case of STRS), and health care contributions made in the post-1999 period for the defined benefit plan, and how that would be expressed.* Perhaps the most difficult suggestion to implement, the proposal addresses this issue by calculating the historical UAL related to ARP membership and fixes that in time, therefore excluding just these benefit changes that could artificially affect the ARP UAL.

The above formula also has the advantage of considering the discrepancy of mitigating rates over time. For example, STRS has had a higher mitigating rate than PERS. As a result, a greater portion of the historical ARP UAL will have been paid by the higher mitigating rate than what has been paid by PERS with its lower mitigating rate, and PERS will likely have a higher historical rate than STRS under the proposed formula. This is an appropriate and fair calculation that reflects the reality of greater UAL payments by ARP employers over the past 15 years to STRS rather than PERS. Conversely, STRS has a greater percentage of its members as ARP participants; therefore STRS' existing ARP UAL will be higher than PERS. Again, the formula captures these differences.

ORSC staff does note some areas needing clarification.

1) The amendment uses the term "perpetual." In the field of actuarial studies this is understood to be a 100-year period. ORSC staff would prefer that the specific period of time be delineated in statute rather than using "perpetual" as a term of art in the Code.

2) The formulation of the subsequent component of the formula (the post-2016 formula) amortizes the amount over a perpetual period. This would more appropriately be amortized over a thirty year period to reflect intergenerational equity instead of pushing that amortization period of existing ARP participants out to 100 years. The post-2016 formula also determines the historical UAL by multiplying the historical percent by the UAL. ORSC staff is not clear on why this extra calculation is made.

3) For the purpose of clarity, we would recommend that the UAL historical calculation specify components that will be used in its calculation. For instance, the calculation should explicitly state that the historical UAL consider already made mitigating rate payments, rather than it being implied.

With some clarifying changes, ORSC staff recommends the implementation of the intent in the proposed formula to bring a resolution to this longstanding issue of contention.

Actuarial impact

H.B. 520 has a number of changes that could have an actuarial impact on the systems. ORSC staff has forwarded these provisions to our actuary for review. A follow up of this analysis will include a general review of the actuarial impact of the bill. This analysis serves as an analysis of the policy portions of the bill to facilitate its progress through the legislature as the policy and actuarial components of the bill are fairly discrete and able to be so divided.

ORSC Recommendation

ORSC staff recommends that the Ohio Retirement Study Council approve of H.B. 520:

1) The bill makes a number of clarifying and administrative changes that improve the operation of the systems.

2) The bill provides a new mitigating rate formula that is consistent and clarifies the intent of the General Assembly. While the intent of the proposed language is apparent, staff recommends clarifying the bill's specific language regarding the use of the term of art "perpetual" and the precise components of the historical UAL. Finally, because the initial calculation may take some time and the effective date of the bill may be delayed, staff recommends that the first calculation be done at the end of 2017, rather than 2016.

3) Under S.B. 42 of the 130th General Assembly, service credit transfers were modified. One modification required that, should PERS transfer credit to OP&F, the member must be eligible to retire and retire within 90 days. This is problematic as it prevents such a member from participating in DROP. This was clearly not the intent of the bill. ORSC staff recommends that an amendment be made to continue to permit those transferring PERS credit to OP&F to participate in DROP.

4) Current law provides that SHPRS DROP participants are "retired" for purposes of electing membership to the Board. Because these individuals remain "active" employees in all other ways, ORSC staff recommends the addition of an amendment to provide that SHPRS DROP participants be treated as "active" for Board election purposes.

This would also make the SHPRS DROP provisions consistent with OP&F as OP&F DROP participants are "active" for purposes of electing membership to the Board.

5) To avoid issues of dispute in a largely administrative bill, ORSC staff recommends the follow two provisions receive additional review and consideration:

a) The total exclusion of employer contributions to an additional annuity for certain "compensation" excluded from being used as a benefit in STRS.¹⁷ *ORSC staff recommends that the exclusion be tied to the withdrawal rate, rather than being set to 0%. The current withdrawal employer match is 50%. If this amendment were added, STRS would increase the amount of employer amounts withheld from these excess contribution from 0% (under current law), to 50%.*

b) Transfer of serviced credit between OP&F, SHPRS, SERS, and STRS. The transfer of service credit regarding non-USERRA military credit and conditions of transfer to OP&F and SHPRS from SERS require additional review and interested party involvement.¹⁸ *ORSC staff recommends this provision receive further review in light of recent service credit transfers between OP&F and PERS.*

6) There are a number of purely technical amendments that ORSC recommends including in any subsequent versions of the bill.

¹⁷ R.C. 3307.501(D).

¹⁸ R.C. 3307.58(A), 3309.73, and 3309.731.