PUBLIC EMPLOYEES
RETIREMENT ASSOCIATION

Date: March 28, 2024
To: Chair Her & LCPR Commission Members
From: Doug Anderson, Executive Director
Amy Strenge, Policy Coordinator
Subject: HF 5137 (Wolgamott) / SF XXXX – Police & Fire Plan Work After Retirement Provisions

Currently, a Police & Fire Plan (the Plan) member may retire, commence a retirement benefit, and then return to work in a PERA covered position if they have had a 30-day break in service and no prearranged agreement for reemployment with their employer. Once re-employed, the member will have a portion of their monthly benefit withheld in a deferral account for later distribution if their earnings exceeds a certain amount ($22,320 in 2024).

HF 5137 / SF XXXX eliminates the above-described break in service requirements and the potential benefit withholdings. A member would simply receive their full retirement and earnings. Similar to current provisions, upon benefit commencement, benefit accruals, employee contributions, and employer contributions all cease.

HF 4553 / SF 4645 is a bill related to work after retirement provisions for the MSRS State Patrol Plan. That bill, as amended, would be similar to HF 5137 / SF XXXX except continuing the employees and employers contributions after benefit commencement until the member terminates employment. At that time, the member would receive a refund of their post-commencement employee contributions with interest, currently at the rate of 3%.

<table>
<tr><th></th><th>PERA P&F
Current Provisions</th><th>PERA P&F
HF5137/SFXXXX</th><th>PERA P&F
HF5137/SFXXXX if amended to reflect HF 4553/SF4645</th></tr>
<tr><td>Break in service required on or after 55?</td><td>Yes (30 Days & No pre-arranged agreement)</td><td>No</td><td>No</td></tr>
<tr><td>Deferral Account</td><td>Yes</td><td>No</td><td>No</td></tr>
<tr><td colspan="4"></td></tr>
<tr><td>Benefit accrual after benefit commencement</td><td>No</td><td>No</td><td>Yes – Refund of EE contributions</td></tr>
<tr><td>EE Contributions after benefit commencement</td><td>No</td><td>No</td><td>Yes</td></tr>
<tr><td>ER Contributions after benefit commencement</td><td>No</td><td>No</td><td>Yes</td></tr>
<tr><td colspan="4"></td></tr>
<tr><td colspan="2">Cost due to higher rates of earlier benefit commencements (members electing to commence benefits at age 55 and remain active)</td><td>$15.2M/year</td><td>$15.2M/year</td></tr>
<tr><td colspan="2">Cost due to cessation of employee and employer contributions to the plan</td><td>$2.1M/year</td><td>$0.8M/year</td></tr>
<tr><td colspan="2">Annual Plan Cost (increases 3%/year for 30 years)</td><td>$17.3M/year</td><td>$16.0M/year</td></tr>
<tr><td colspan="4"></td></tr>
<tr><td colspan="2">Present Value of higher benefit costs plus loss of future contributions</td><td>$290M</td><td>$206M</td></tr>
</table>

What are the current earnings threshold and deferral account rules?
After reemployment, if a member's earnings from a PERA covered employer in any given year exceed a threshold ($22,320 in 2024) a portion of their monthly benefit is withheld by the Plan in a deferral account, without interest. The amount withheld is returned to the member the January following the calendar year after the amount is withheld (ex. 2024 withholdings are distributed in January 2026).

Why is this cost more than expected?
The estimated cost impact is higher than originally expected due to both the favorable benefit impact to the member and the loss of contributions for the period from age 55 to the actual retirement age, if later than 55. The proposed change would not just increase Plan costs for the hoped for additional retention period, it would also increase costs for the existing period of employment already occurring after age 55 for many members.

How is this change favorable to the member?
Currently, when active members retire after the normal retirement age, the increased Plan liability associated with a higher benefit amount commencing later is more than offset by a reduction in their payout period due to the delayed commencement. Furthermore, the member continues to contribute. If an earlier option is available to commence benefits and cease contributions, the member will benefit and the Pan's liability will increase.

Does this study reflect recent actual rates of retirement?
Data analysis from fiscal year 2023 confirms anecdotal evidence of higher rates of earlier retirement than currently assumed in actuarial valuations. A revised baseline assumption reflecting the higher early retirement rates was developed for the purposes of this study.

What impact does higher earlier retirement rates have on the plan?
Earlier retirements will translate to higher plan costs, whether or not the proposed plan change to an in-service distribution model occurs. The estimated cost impact resulting from the revised baseline assumption is about 0.8% of payroll, which is about $10M/year. The revised baseline also means about $1M/year fewer contributions to the Plan. The 4-year experience study will refine this assumption. However, it is reasonable to expect that the general trend towards earlier retirements will have an adverse cost impact to the Plan, even without any change in work after retirement provisions.

How do these proposed changes impact member behaviors and plan costs?
The proposed change introduces an election option for the active members making it easier to commence a benefit. This may happen in the following ways:

1. A member intending to retire at age 55 and uncertain about later reemployment in a PERA covered position (after a break in service) could now more easily resume employment and receive their benefit without benefit deferment. In this instance the benefit commencement rate is increased, and an additional period of employee retention has been achieved.
2. A member already planning a retirement later than age 55 could now start their benefit at 55 rather than waiting for their retirement age. In this case, the expected PERA employment period is the same, but the benefit commencement is earlier. In this instance the benefit commencement rate is increased but an additional period of employee retention has not been achieved.

In both cases above, the benefit commencement date is likely to occur earlier than previously assumed. In both instances, the Plan will incur costs, but only in the first instance has employee retention improved. **This proposed change may help with retention by prolonging careers after normal retirement age (at an increased cost to the Plan). However, it also increases the cost to the Plan for members working after retirement that will not choose to work longer.**

What assumption was used for this study?

Evaluation of costs now require that we separate the retirement age assumption and the benefit commencement age assumption. The benefit commencement age assumption is now critical to cost evaluation. As noted above, if members make their decisions solely on the present value of their pension benefit, commencement at age 55 would be the most attractive option in most instances.

The cost study is based on the assumption that there will be a 50% increase in retirements at and above Normal Retirement Age (age 55). If this assumption is too low, retention of members and actual costs will be higher than estimated. If the assumption is too high, retention of members and actual costs will be lower than estimated.

What is the cost impact of eliminating the deferral account?

In addition to the above cost estimates, the elimination of the deferral account would adversely impact the fund. Currently the Plan retains about $3M per year on about 130 deferral accounts. The estimate annual investment earnings retained by the fund on these member's benefits is about $200,000/year.

What conclusions can be made?

The cost study revealed several important considerations:

1. Under current provisions, delaying retirement after age 55 is helpful to Plan funding due to delayed payments and continuing contributions. These amounts are more than the cost of the increased benefit amount the member will eventually receive.
2. Retirement after age 55 is not uncommon. There are currently over 600 active members over age 55. Prior to 2020 roughly half of members continued working after age 55.
3. Data analysis confirms that members are retiring earlier post 2020 than before 2020.
4. Members may benefit considerably by being able to commence their benefit at age 55 due to both earlier benefit commencement and cessation of their contributions.
5. The proposed change may help with retention by prolonging careers after normal retirement age (at an increased cost to the Plan). However, it also increases the cost to the Plan for members working after retirement that will not choose to work longer.

The reason for the cost study was to estimate the cost impact to the Plan if members are retained for a longer period. The focus was originally on an assumed narrow group of members. However, the cost study revealed that this bill potentially has a much larger impact on how benefits and costs are impacted for a relatively large group of members retiring after age 55. The study also revealed that the next experience study may result in higher Plan cost estimates due to earlier retirements regardless of whether the proposed change becomes effective.