Summary of the TMRS Advisory Committee on Benefit Design Interim Session

October 20, 2016

TMRS Board of Trustees

TMRS
Texas Municipal Retirement System

Advisory Committee Charge / Desired Outcomes

- Provide input to the Board on the advantages and disadvantages of benefit design issues affecting TMRS cities, members, and retirees as assigned by the Board;
- Provide an additional conduit for communication between the Board and its members, retirees, city officials and policy makers;
- Maintain communication with statewide professional organizations, including employer and employee groups, and member cities.

Interim Session Activities

June 23, 2016 – Advisory Committee Meeting #1

- Receive education from TMRS Actuary (GRS) and Staff on study issues
- Consider, discuss and develop the advantages and disadvantages of each study issue
- Request additional information as needed

Between Advisory Committee Meetings

- Individually consider and respond to a possible survey from TMRS staff regarding the study issues
- Review and consider materials provided in response to information requests
- Contact TMRS staff with any requests for clarification or further information

August 18, 2016 – Advisory Committee Meeting #2

- Review the results of the Committee survey and materials provided in response to information requests
- Further consider and discuss study topics
- Finalize the list of significant advantages and disadvantages of each study topic

Discussion of Legislative Agenda

Follow-up to September Board Meeting

- Return to Work Trends
- COLA / Catch up Provision City Survey
- Options for Board to Consider

Study Topic Overview – Return to Work and COLA/Catch-up Provisions

October 20, 2016

GRS
Gabriel Roeder Smith & Company
Consultants & Actuaries
www.gabrielroeder.com

Return to Work (RTW) Policies

- Managing policies that apply to employees who have retired and then choose to return to work (RTW) for the former employer creates challenges for all public employee retirement systems

TMRS current provisions

- Currently, if a member retires from one city and then returns to work for that same city:
  - The member's current annuity is suspended until he re-retires (the member forfeits the benefit payments that would have occurred during the suspension)
  - A new member account is created to which the member and employer contribute (with interest granted) and the balance is annuitized at the second retirement

TMRS current provisions

- There is a special provision for members who are separated from their employer for a period of more than 8 years before they return to work. Those members are eligible to receive as a lump sum the accumulation of their suspended benefit payments when they re-retire (without interest)

TMRS current provisions

- When a member returns to another TMRS city, the member's annuity is not suspended and they can simultaneously receive their annuity from the previous city and salary from their new city
- A new member account is created to which the member and employer make contributions like any other member (with interest granted) and the balance is annuitized at the second retirement

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Length of separation

- There are IRS requirements addressing a “bona fide” break in service and no pre-arrangement for re-hire
- While there are no specified definitions, general opinions are that at least a 6-month separation is needed, with 1 year being safer
- The 1 year requirement is less likely to cause a change in behavior than a shorter requirement
  - Makes it harder for an employer to guarantee position
- We have estimated that if new provisions were enacted that increased retirement behavior by 20%, the average increase in employer rates would be from 0.03% to 0.13%

Who should new provisions apply to?

- Just future retirees?
  - Low to no cost, loss of future gain
- Current retirees who have yet to return to work?
  - Low to no cost, loss of future gain
- Retirees who have returned to work but have not re-retired?
  - Provide prospective only or include retro payments?
  - On a prospective basis: low cost, loss of future gain
  - Providing retrospective payments will have a cost, with a wide distribution based on the utilization at the given City
  - Some cities may have previously benefited from actuarial gains
- If retrospective payments are provided, what about the retirees who have previously returned to work but have already subsequently retired?

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Basic Considerations

- In all scenarios, recommend no change to the current treatment for new accruals
  - Member contributes into a new account
  - Employer provides a match
  - Earns interest just as any other member
  - Any USC calculation is only based the new employment period
  - Balance is annuitized at second retirement based on age at second retirement. Any option is available.
  - No change to original annuity, except for perhaps COLAs granted during the reemployment

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Options for Original Annuity during re-employment

- Option 1: Treat RTW retirees at previous city after a 1-year break in service just like a member who returns to a different city
  - No suspension, continue to receive annuity
  - By far the least administrative burden compared to current policy
  - Puts previous employer in same position as another employer

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Options

- Option 2: Decrease the 8 year requirement to 1 year
  - Annuity is suspended, but accumulated suspended payments are paid to the retiree at the subsequent retirement without interest
  - The second least administrative burden compared to current policy
  - Attempts to make the member whole compared to value before second employment
  - Ensures that a member who retires and returns to work does not receive an enhanced benefit compared to the member who never retired

Options

- Variants of Option 2: Decrease the 8 year requirement to 1 year
  - Could provide interest on suspended payments
    - Provides even greater incentive to return to work
    - Could lead to more pronounced impact on retirement behavior with potential significant costs
  - Could annuitize accumulated balance (with or without interest) of suspended payments
    - Annuitized based on age at second retirement using same option as the original annuity
    - Added to the original annuity
    - Member would ultimately receive total of:
      - Original Annuity (at original option, with COLAs)
      - Annuity of Suspended Payments (at original option based on current age)
      - Annuity for new employment (any option based on current age)

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Example

- Member retires at age 55 with a $40,000 annual benefit ($3,333 per month)
- Returns to work at age 56 and works for 5 years, retiring a second time at age 61
  - Receives $422 per month in additional annuity based on second 5 year employment
- Based on current provisions, the $3,333 would recommence at the second retirement with any COLAs granted during the suspension period
- In all scenarios, the member receives their salary from their employer

Example

- Under option 1 (no suspension), the member would receive their annuity and their salary during the re-employment period and then have the $422 added to their annuity at the second retirement
- Under option 2 (suspension but accumulation of missed payments), there are the following alternatives at second retirement (plus the $422 increased annuity)

	Lump Sum	Increased Monthly Annuity
Without interest	$200,000	$1,212
With 5% interest	$226,551	$1,373

Under the with interest scenario, the member would receive $3,333 plus $422 plus $1,373 = $5,128 monthly

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Current COLA Options

- 30%, 50% or 70% of CPI-U
- Repeating COLAs are advance funded over each active employee's working career
- Ad-hoc COLAs are funded when granted over 15 years with level dollar amortization

COLAs are Retroactive

- Increases are calculated as if COLA had always been in effect since date of retirement
  - Typically referred to as "catch up" provision
- Initial COLA or an increase in CPI percent results in large benefit increases for the year adopted; longer retired, higher the increase
- Reduction in CPI percent results in lower or no increase until cumulative increase at lower percent exceeds current benefit; longer retired, longer until another increase will be granted
- Two alternatives have been proposed that would eliminate the retroactive or catch up feature:
  - Current CPI based COLA without retroactive feature
  - Flat rate COLA of a specified percentage increase

Ad hoc Comparative Analysis 1 – COLA last adopted January 2010

	Baseline * (No COLA)	70% CPI Ad hoc with Catch-up (6.67%)	70% CPI Ad hoc without Catch-up (0.51%)	Flat 2.5% Ad hoc
UAAL	$60,062,834	$72,868,402	$61,104,951	$65,161,254
Funded Ratio	86.3%	83.9%	86.1%	85.3%
ER Current Service %	7.23%	7.23%	7.23%	7.23%
Prior Service %	5.17%	6.81%	5.30%	5.82%
Full Rate	12.40%	14.04%	12.53%	13.05%
Estimated Contribution	$10,399,826	$11,775,287	$10,508,856	$10,944,978
Annual Cost to Provide COLA		$1,375,461	$109,030	$545,152
Projected CY2017 Benefit Payments	$20,946,533	$22,343,091	$21,053,570	$21,470,196
Increase Due to COLA		$1,396,558	$107,037	$523,663

* City last adopted a COLA on January 1, 2010

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Repeating Comparative Analysis 1– COLA last adopted January 2010

	Baseline * (No COLA)	70% CPI** Repeating with Catch-up (6.67%)	70% CPI** Repeating without Catch-up (0.51%)	Flat 2.50% Repeating COLA
UAAL	$60,062,834	$146,419,293	$132,699,102	$167,458,448
Funded Ratio	86.3%	72.1%	74.1%	69.3%
ER Current Service %	7.23%	9.34%	9.34%	10.24%
Prior Service %	5.17%	11.68%	10.64%	13.27%
Full Rate	12.40%	21.02%	19.98%	23.51%
Estimated Contribution	$10,399,826	$17,629,382	$16,757,138	$19,717,734
Annual Cost to Provide COLA		$7,229,556	$6,357,312	$9,317,908
Projected CY2017 Benefit Payments	$20,946,533	$22,343,091	$21,053,570	$21,470,196
Increase Due to COLA		$1,396,558	$107,037	$523,663

* City last adopted a COLA on January 1, 2010

**Assumes CPI will increase 2.5% annually

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Ad hoc Comparative Analysis 2– COLA never adopted

	Baseline * (No COLA)	70% CPI Ad hoc with Catch-up (10.32%)	70% CPI Ad hoc without Catch-up (0.51%)	Flat 2.5% Ad hoc
UAAL	$21,413,900	$27,155,999	$21,767,835	$23,145,480
Funded Ratio	91.0%	88.8%	90.9%	90.3%
ER Current Service %	4.90%	4.90%	4.90%	4.90%
Prior Service %	3.00%	3.88%	3.05%	3.27%
Full Rate	7.90%	8.78%	7.95%	8.17%
Estimated Contribution	$5,545,153	$6,162,841	$5,580,249	$5,734,671
Annual Cost to Provide COLA		$617,688	$35,096	$189,518
Projected CY2017 Benefit Payments	$6,601,287	$7,282,614	$6,635,019	$6,766,319
Increase Due to COLA		$681,327	$33,732	$165,032

* City has never adopted a COLA

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Repeating Comparative Analysis 2 – COLA never adopted

	Baseline * (No COLA)	70% CPI ** Repeating with Catch-up (10.32%)	70% CPI** Repeating without Catch-up (0.51%)	Flat 2.50% Repeating COLA
UAAL	$21,413,900	$69,574,123	$63,328,054	$82,437,140
Funded Ratio	91.0%	75.7%	77.3%	72.4%
ER Current Service %	4.90%	6.60%	6.60%	7.32%
Prior Service %	3.00%	7.33%	6.77%	8.49%
Full Rate	7.90%	13.93%	13.37%	15.81%
Estimated Contribution	$5,545,153	$9,777,720	$9,384,646	$11,097,326
Annual Cost to Provide COLA		$4,232,567	$3,839,493	$5,552,173
Projected CY2017 Benefit Payments	$6,601,287	$7,282,614	$6,635,019	$6,766,319
Increase Due to COLA		$681,327	$33,732	$165,032

* City has never adopted a COLA

**Assumes CPI will increase 2.5% annually

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Presentation of Committee Identified Advantages and Disadvantages

TMRS
Texas Municipal Retirement System

Return to Work Option 1 Description

After a 1-year break in service, do not suspend the benefit, but treat employee the same as if he/she were going to work at a city other than the last-employing city. The retiree continues to receive his/her benefit payments and his/her salary while employed.

Return to Work Option 1: Committee Identified Advantages/Disadvantages

Summarized Advantages	Summarized Disadvantages
1. More consistent with rules for going back to work with a different city	1. Does not completely level the playing field for the employer
2. More consistent with private sector rules and practices	2. Allows the city an opportunity not to fill that position with a promotion or a new hire
3. One year break in service is fair, and is better than other statewide plans	3. With only a one-year year break, could be abused by some employees/employers
4. Simple to understand	4. Seems to stray further from the objective of TMRS to administer retirement benefits
5. Eliminates the preferential carve out for employees retired at least eight years	5. Possibility of negatively affecting retirement patterns for TMRS as a whole is greater

Return to Work Option 1: (continued) Committee Identified Advantages/Disadvantages

Summarized Advantages	Summarized Disadvantages
6. Allows the city to compete for the services of that retiree on a level playing field, providing more workforce flexibility	6. TMRS administrative burden (as would exist with any change)
7. Fiscal impact on cities would be insignificant since the payout would not change	7. May affect city contribution rates and COLA provisions
8. One-year break-in-service is more defendable against accusations of “double dipping”	8. Although the TMRS benefit is an earned benefit, could be perceived by the Legislature and public as “double dipping,” possibly bringing negative attention on both TMRS and municipal employers
9. Doesn’t have a negative impact to the TMRS system	

Return to Work Option 2 Description

After a 1-year break in service, the retiree could return to work at the last-employing city, have his/her annuity suspended but have his/her annuity, including any COLAs granted during the period of suspension, held in an account and paid as a lump sum payment, with or without interest, or re-annuitized upon his/her re-retirement.

Return to Work Option 2: Committee Identified Advantages/Disadvantages

Summarized Advantages	Summarized Disadvantages
1. Eliminates the preferential carve out for employees retired at least eight years	1. Treats the retiree differently than any other private or public employer
2. Lifts penalty for returning to work after a reasonable separation period without a penalty and true loss of annuity payments already earned	2. TMRS administrative burden (as would exist with any change)
3. Reduces the retirees' concerns that he/she retired too early or at the wrong time	3. Some employers/employees could possibly take advantage of the system
4. Allows the retiree's city to compete for the services of that employee on a level playing field, and provides cities more workforce flexibility, particularly for those in geographically isolated areas and for those who have "key knowledge" positions	4. Allows the city an opportunity not to fill that position with a promotion or a new hire

Return to Work Option 2: (continued)
Committee Identified Advantages/Disadvantages

Summarized Advantages	Summarized Disadvantages
5. Although the TMRS benefit is an earned benefit, this option is less likely to be perceived by the Legislature and public as “double dipping”	5. Possibility of negatively affecting retirement patterns for TMRS as a whole
6. Fiscal impact on cities would be insignificant since the payout would not change	6. May affect city contribution rates and COLA provisions

Return to Work: Additional Considerations

- To whom would such a provision apply?
  a) Future retirees only?
  b) Those who have already retired but have yet to return to work at their last-employing city?
  c) Those retirees who have already returned to work for their last-employing city with less than an eight year break in service?

COLA/Catch-up Option 1 Description

Allow cities to adopt a COLA (either ad hoc or repeating) at 30%, 50%, or 70% of CPI based only on the change in the CPI in the most recent year. In other words, allow a city to adopt a COLA that does not include the catch up feature.

COLA/Catch-up Option 1: Committee Identified Advantages/Disadvantages

Summarized Advantages	Summarized Disadvantages
1. Removes an administrative obstacle while retaining local control, local fiscal responsibility, and providing flexibility that is currently lacking	1. Allowing cities to opt in and out of or reduce their COLA without some type of limitation may eventually create unintended consequences to the System overall
2. Makes it easier for cities to plan for the COLA, and adjust to annual budget challenges	2. Ease of change; the COLA is an expensive proposition, even without the retroactive provision
3. Tied to cost of living as opposed to being arbitrary	3. Could put retirees more at risk to unknown future changes in their monthly pension; ultimately could lead to lower benefits over time
4. Might encourage some cities to offer a COLA or restore a partial COLA where one hasn't been offered or has been discontinued, thereby increasing the total percentage of TMRS annuitants receiving a COLA	

COLA/Catch-up Option 1: (continued) Committee Identified Advantages/Disadvantages

Summarized Advantages	Summarized Disadvantages
5. Modernizes the COLA option in a common sense, simple to understand way	
6. Will not affect cities providing current COLA benefits	
7. All Retirees will see an increase because the catch-up feature is not included	
8. Provides one additional feature for cities to use to recruit and retain talent	
9. Creates consistency among an employer's salary adjustment practices between actives and retirees (i.e., actives do not receive retroactive salary adjustments for prior years without an increase)	
10. Defendable with the Legislature	

COLA Option 2 Description

Allow cities to adopt a COLA (either ad hoc or repeating) at a flat rate based on a percentage of the retiree's annuity. In other words, a COLA not tied to the CPI change, 5% for example, subject to IRS limitations. By definition, a flat rate COLA does not have a catch-up feature.

COLA/Catch-up Option 2: Committee Identified Advantages/Disadvantages

Summarized Advantages	Summarized Disadvantages
1. Gives cities an additional COLA option	1. Not defendable with the Legislature and the public
2. Removes an administrative obstacle while increasing local control and local fiscal responsibility	2. Does not encourage sustainable COLA patterns over the long term and might jeopardize the opportunity for retirees to receive future COLAs because they are easy to discontinue
3. May provide the greatest flexibility for cities as long as the catch-up feature is not applied	3. Some employers could possibly take advantage of the provision, which could lead to criticism, especially if the flat rate percentage is an amount that is viewed as unacceptable

COLA/Catch-up Option 2: (continued)
Committee Identified Advantages/Disadvantages

Summarized Advantages	Summarized Disadvantages
4. Allows a city to better manage current resources while still providing an annuity increase to retirees	4. Allowing cities to opt in and out of the COLA without some type of limitation may eventually create unintended consequences to the System overall, such as less retirees overall receiving a COLA
5. Understandable and a possibly a better benefit to retirees than the current COLA provision	5. COLA granted may not be reflective of inflationary conditions causing the COLA to fall short at times, potentially for long periods, without improvement

Open Discussion and Next Steps

- What questions does the Board have about the Committee's discussions or work product?
- What additional information would aid the Board in assessing these topics (e.g., additional surveys, peer research, a presentation by the Board's Legislative consultant, etc.)?