TMRS Advisory Committee on Benefits Design
Meeting Summary
June 23, 2016

The TMRS Advisory Committee on Benefits Design (the "Committee") met on June 23, 2016 at TMRS Headquarters in Austin, TX for the first of its two scheduled meetings during this interim. The purpose of this first meeting was for Committee members to 1) receive education from the System's actuary regarding the two study topics assigned by the TMRS Board of Trustees: return to work and COLA provisions, 2) share their early views on the possible advantages and disadvantages of the study topics, and 3) request additional information that would assist the Committee in its subsequent proceedings.

This summary is intended to convey the primary themes addressed during each of the four major segments of the meeting. The Committee's meeting materials are available on the TMRS website. More detailed meeting minutes will be available in August after they are approved by the Committee.

Please contact TMRS staff at 512.476.7577 or 800.924.8677 with any comments or questions.

I. Committee Welcome and Opening Remarks

Members of the Committee were welcomed to the proceedings by TMRS Board Member and Committee Chair Bill Philibert. Each Committee member introduced himself or herself, and guests in the audience were recognized. The Committee was reminded that there have been recent Board-adopted changes to the Committee charter to enhance the effectiveness of input to the Board. In connection with this, the overall goal of the interim study sessions was articulated for the Committee to provide the Board with a compilation of advantages and disadvantages of each of the two study topics. The value of the Committee's historical objectives of serving a broader role as a communication conduit between the Board and stakeholders was reemphasized and remains unchanged.

The Board's rationale for selecting the two specific study topics was shared. Although the Board has not formally specified) any next steps at this time, there has been much Board interest to receive a deeper and more comprehensive understanding of stakeholder perspectives regarding the two study topics. The Committee's work, along with other information, will assist the Board as it reviews possible actions in the future.

II. Presentation and Discussion on TMRS Return to Work Provisions

Joe Newton of Gabriel, Roeder, Smith & Co. ("GRS"), the Consulting actuary, provided an educational presentation to the Committee. He discussed the challenges for public retirement systems like TMRS in managing return to work provisions. Provisions can either be cost neutral or add cost to the employer's plan, depending upon whether the provisions result in changes in retirement behavior.. In other words, if a return to work policy encourages more employees to

retire earlier in anticipation of being able to return quickly to work after retirement, then the provision can increase plan costs.
Provisions that are viewed as "lenient" can increase political and public criticism of "double dipping". Some public retirement systems have features that can contribute to this view, such as a very short break in service[1], or very favorable treatment of benefit accrual and compensation during the time when the retiree returns to work.

Current TMRS provisions were then described. The parameters of the current TMRS return to work provision are different depending upon whether a retired member returns to work at the city of last employment or goes to work at another city. If a member returns to work at the city of last employment, the monthly retirement benefit is suspended and forfeited while re-employed. The exception to this is if eight years have passed between the time of retirement and returning to work with the same employer. If this occurs, payments are still suspended but are returned at the retiree's subsequent date of retirement. In contrast, if a retiree goes to work at another city after a bona fide separation from the prior city and retirement[2], there is no benefit suspension. TMRS Director of Actuarial Services, Leslee Hardy, presented data regarding the number of members affected by this provision as of December 31, 2015. She noted that while only a small percentage of retirees have returned to work, the number has increased over the past several years.

National trends were also presented. They range from suspending a benefit to allowing in-service distributions. If benefits are suspended, most plans do not accumulate and pay out the value of forfeited payments at the member's second retirement. The most common practice is that a minimum break in service threshold must be met before the annuity and salary can both be received; if the minimum threshold is not met, the benefit is suspended.

There were several stated reasons as to why the topic of return to work is appropriate to discuss now. Broader demographic and economic trends were explained. The aging workforce is a well-recognized phenomenon. Healthcare costs continue to rise and, in turn, are becoming an increasingly larger retirement expense. Additionally, legislation has been proposed in past sessions to alter the current TMRS provision. A historical view of the provision and recent related legislation and its outcomes was presented by Dan Wattles, TMRS Director of Governmental Relations. The likelihood of having an unfavorable Legislative outcome on perceived benefit enhancement legislation was discussed given the political climate.

[1] The period of time in which a member needs to be "separated from service" before he or she can be rehired by the same employer.
[2] If there is no break in service from a city employee – that is, if the employee begins work directly for another city after leaving the prior city – it may affect the retirement application of a TMRS member. TMRS does not allow for in-service distributions of retirement annuities.

The Committee next heard about specific features of return to work that are to be studied, including returning to work at the city of last employment, length of separation of service, annuity suspension versus accumulation of suspended payments, interest or no-interest on suspended amounts, and lump sum versus annuitization of the balance of the suspended payments since the member returned to work. Impacts of the features on behavioral retirement patterns due to length of separation were explained, as well as how different behavioral scenarios can drive employer costs.

Finally, it was noted that although the IRS has recently issued guidance on normal retirement age for governmental plans and in-service distributions, there is no bright line definition for the length of time that constitutes a bona fide separation from service. On a national basis, public retirement system practices range from shorter periods such as thirty-days to longer periods of a year or more. GRS recommended at least a one year separation period.

Discussion

The three primary options presented for Committee evaluation and discussion were as follows:

	Option 1	**Option 2**	**Option 3**
Description	No change to the current provision	After a 1-year break in service, treat the retiree the same as if he or she were going to work at a different city (retiree continues to receive his or her benefit payments in addition to salary)	Decrease the current 8-year break in service requirement to 1-year, suspend the benefit during the period of re-employment, and make the employee whole to some extent upon re-retirement, either by providing interest on suspended payments or just suspended payments through a lump sum payment or annuitization based on the original retirement option at current age
Estimated cost impact[3]	No change in city contribution rates expected	Little to no effect if only applied prospectively; similar effects	Impact to employer cost depends upon who the provision is extended to: a) Only future retirees; low to no cost. b) Current retirees who have yet to return to work; low to no cost.

[3] All three scenarios assume that the retiree rejoins TMRS and participate in new accruals upon return to work.

	Option 1	**Option 2**	**Option 3**
		to option 3 if provided retroactively	c) Retirees who have already returned to work but haven't yet re-retired; if applied on a prospective basis, low cost; if applied retroactively, there will be a wide range of costs based upon city specific utilization d) Retrospective payments to retirees that have returned to work and already re-retired; wide range of costs reported based upon city specific utilization; should be considerable higher than (c)

Committee members provided their initial views and questions on the topic, as follows:

- While the actual number of TMRS retirees affected to date appears to be small, the aging of the workforce coupled with rising healthcare costs is likely to significantly increase its impact going forward.
- There was some coalescence around Option 2 with a number of Committee members noting that it provides the cities the option to increase their employment pool; it is cost neutral if applied prospectively, it removes the perceived inequality for the member, and levels the playing field for rehiring retirees across different TMRS cities.
- Some Committee members who voiced support for Option 2 offered possible cost mitigating enhancements to consider, such as a salary threshold or cap or a length of service requirement.
- A few members favored Option 3, noting that a member is not "double dipping" during the re-employment period, but is made whole later for the suspended annuity payments without creating an incentive for re-employment after retirement.
- The definition and negative perception of the term "double dipping" was discussed. Some noted that it is common for people to work in retirement, whether it is in the private sector or public sector.
- Some members were not in favor of trying to advance this provision at this time and preferred the status quo, particularly in light of the anti-double dipping legislation during the last Legislative session that affected elected state officials. They emphasized the need to demonstrate a compelling reason for change on the employers' behalf. Others believed that in combination with the COLA provision, now might be the right time to bring the legislation forward.
- Several members discussed how health care costs for a retiree or retiree's spouse may force a retiree to return to work and asked if it might be possible for a qualifying event to trigger a change to the annuity suspension terms, but the committee discussion focused

more on uniform RTW provisions rather than provisions triggered by certain events for certain retirees.

As part of the discussion wrap up, the Committee was asked to consider the objective it is trying to address; making the member whole, or creating some equality with the current provisions that apply to re-employing cities. There were mixed Committee member viewpoints as to which objective was more important, with some wanting to address the benefit forfeiture aspect and others wanting to continue to control costs and reduce any competitive disadvantage for a city that wishes to re-employ one of its retired employees.

III. Presentation and Discussion on TMRS COLA and Retroactive Provisions

Mr. Wattles provided a history of legislative actions regarding COLAs, noting that there has been a COLA bill in each of the last four sessions (not TMRS sponsored). Mr. Newton presented a brief educational backdrop to the Committee on COLAs, noting that COLAs were extensively reviewed by the Committee in 2014. He reviewed the current TMRS COLA options, and provided a short-term analysis of cities that have adopted ad hoc versus repeating COLAs. He noted the differences in funding approach, funded ratios, cost increases, and reporting requirements. The long-term analysis demonstrated that the cumulative contributions for regular, yearly ad hoc COLAs exceed those for repeating COLAs due to prefunding and earned interest. Some Committee members expressed a need for better education of city decision-makers.

The retroactive "catch up" feature of the COLA was then explained and defined. Mr. Newton presented his view of the advantages and disadvantages of non-retroactive COLAs as follows:

<u>Advantages</u>

- Provides an additional option for cities
- Can help better control costs
- Can help dampen liability growth
- Costs less because the benefit is smaller

<u>Disadvantages</u>

- May not keep pace with CPI
- Does not restore lost purchasing power
- Adds administrative complexity

<u>Discussion</u>

Scenarios were then presented to the Committee for comparison and discussion including:

- CPI versus flat-rate COLAs;
- Costs to a city of an ad hoc COLA, both with and without catch-up and a flat rate;
- Repeating COLAs, with and without a catch-up and a flat rate; and

- Cost impact for a city that has never adopted a COLA, with and without a catch-up and flat rate, both on an ad hoc and repeating basis.

To seek initial input, some Committee members suggested that the Committee first frame the primary objective to be addressed. The competing interests of compassion in providing purchasing power assistance during retirement and cost control were noted. Additional comments on these themes included the following:

- If the current statute and provision in effect discourages COLA adoption due to cost, the Committee may want to focus its efforts on addressing this.
- A number of Committee members agreed, identifying the catch-up feature as the entry barrier for cities that have turned off the COLA or never adopted one.
- Removing the retroactive catch-up feature may be helpful to cities, but discipline to advance fund the COLA cost is still key.

IV. <u>Session Recap – Request for Information</u>

Several requests for additional information arose during the Committee's discussions on both study topics, as follows:

- Gather and present data, to the extent possible, on why retirees were rehired by their city and what job levels they were rehired at. Was the rehire city or employee initiated?
- Provide descriptive information on the practices and treatment of COLAs in other Texas statewide public retirement systems
- Provide a list of TMRS cities that have never adopted COLAs, including the number of retirees and ratio of actives to retirees
- Present data to demonstrate whether the TMRS catch-up feature is unique.

These information requests will be fulfilled prior to the next Advisory Committee meeting on August 18, 2016. It was noted that TMRS staff may be reaching out to Committee members to conduct a possible survey on the study topics. Committee members were encouraged to contact TMRS staff to share experiences on these study topics or make additional information requests.

After a brief public comment period, the Chair and Vice Chair of the Advisory Committee thanked the Committee members for their thoughtful, engaged participation, and adjourned the meeting.