OHIO PUBLIC EMPLOYEES RETIREMENT SYSTEM
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www.opers.org

MEMORANDUM

DATE: July 9, 2004

TO: OPERS Retirement Board Members

FROM: Dan Drake, Director – Benefits Administration
             Beverlon Hodge, Asst. Director – Benefits

RE: **IV.   Discussion Item:**
             A.   PLOP Payments Being Used to Purchase Service Credit

Issue:

Currently, when a member applies for retirement and elects a Partial Lump Sum Option Payment (PLOP), the PLOP payment is issued at least 30 days after the first benefit payment.   However, members have at least 180 days after receiving their first benefit payment to purchase additional service credit before their retirement benefit is finalized. The benefit is then finalized using the increased service credit. There is a concern that members may be opting for the PLOP, rolling it over to another trustee, and then rolling these same monies back to OPERS to purchase additional service credit. Or, a member could simply request their PLOP be issued as a direct rollover to purchase service credit. This would result in an OPERS to OPERS direct trustee-to-trustee transfer.

Background:

With the passing of the Economic Growth and Tax Relief Reconciliation Act (EGTRRA), beginning in January 2002, governmental defined benefit plans were given the authority to accept rollover monies from other plans such as supplemental retirement plans (Section 457), defined contribution plans (Section 401(a)), and Individual Retirement Accounts (IRA's). These monies may be used for redeposits, service purchases, or they may be deposited into an additional annuity account.

Since the passage of EGTRRA, members have become increasingly aware of the many avenues now available in using rollover monies to purchase service. In the two years prior to EGTRRA, OPERS processed 236 service credit purchases using rollover monies totaling approximately $3.1 million. As of January 2002, OPERS has processed 2,392 service credit purchases totaling approximately $26.4 million.

Cost of purchasing service credit:

Under statute, the cost of purchasing service credit varies by type. Members may pay as little as $0 (free military, BWC) or as much as 20% times the member's earnable salary for the past twelve months (School Board, Exempt). The 20% rate for School Board and Exempt service represents an approximation of the full liability for both the employee and employer portion of the service. Military service is set at a rate of 10% which provides for only ½ of the liability. Other purchases, such as Redeposits and Out of State only require employee contributions plus interest (currently 6%). Although OPERS applies a variety of formulas depending on the service, other retirement systems utilize the same formula for all service types. For example, STRS applies a 50% liability rate to all service purchases regardless of type.

Using examples provided by Staff, GRS has provided an estimate of the additional liability associated with some of the more common types of service purchases (see attached GRS analysis). More than 1/3 of the service purchased is for redeposits. Purchased military service is slightly less than 1/3. Other types of purchases include exempt, out of state, and elective officials 35%.

The true cost was estimated by computing a weighted average of present value increases at various possible termination ages. Per GRS, analysis shows that for every $ received from the member, there is a cost of approximately $1.91 to OPERS. Thus, if $10 million was received from members for service purchases, the cost to OPERS would be about $19.1 million per year. Based upon a total payroll of $11 billion, this would amount to an annual cost of approximately 0.17% of payroll.

As we move forward some alternatives would be:

1. Not allow members to use PLOP to purchase service
2. Allow members to use PLOP but change the cost of service credit in statute
3. Allow members to use PLOP but make no changes to the cost of service credit in statue

Discussion:

Staff would like to seek input from the Board regarding this issue.

July 7, 2004

Ms. Beverlon Hodge
Ohio Public Employees Retirement System
277 East Town Street
Columbus, Ohio 43215-4642

    Re: Combined Effect of PLOP and Service Purchase subsidy.

Dear Beverlon:

Subsequent to EGTTRA, you have indicated that the incidence of purchased service via rollover has increased as shown below.

	Money Spent on Service Purchases ($Mill)	No. Members Who Purchased Service
2000	1.4	108
2001	1.7	128
2002-May, 2004	26.4	2392

You have asked for an estimate of the cost to PERS of permitting these rollovers. In order to prepare this estimate, we examined a representative cross section of 10 recent cases that you supplied. Our analysis shows that for every $ received from the member, there is a cost of approximately $1.91 to PERS. Thus, if $10 million was received from members for the purchase of service credit, the cost to PERS would be about $19.1 million per year. Based upon a total payroll of $11 billion, this would amount to an annual cost of approximately 0.17% of payroll.

We have attached the output from the spreadsheet you supplied with the ten representative cases. A column was inserted to show our estimate of the "true cost" of the service in each case. This value was determined by computing a weighted average of present value increases at various possible termination ages. Please note the actual cost of additional service will be determined by the actual termination date and the final average pay at that time. Actual results could vary significantly from our estimates.

In addition, the "true cost" values provided for these 10 cases do not reflect any possible cost increases related to non-pension benefits that may also be affected by purchased service (e.g. retiree medical benefits).

Sincerely,

Randall J. Dziubek

Cc: Danny L. Drake
        Laurie F. Hacking
        Norman L. Jones
        Brian B. Murphy
RJD: bbm