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Ohio's Public Retirement Systems

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The retirement systems

Most of Ohio's state and local government employees are required to be members of one of the state's five public retirement systems. Cincinnati has a separate system for its employees, and some employees of public institutions of higher education are permitted to join alternative retirement plans. Participants in all of these systems and plans contribute a percentage of their compensation to fund retirement benefits and, in most cases, disability, survivor, and health care benefits as well. Employers also contribute an amount equal to a percentage of each employee's compensation. Retirement system members do not contribute to Social Security for their government service and those who qualify for a Social Security pension based on other service may have Social Security benefits reduced under federal law known as the "Windfall Elimination Provision."¹

Four of the five state systems cover specialized groups of primarily local-government employees. These systems and the employees they cover are as follows:

State Teachers Retirement System (STRS) — public-school employees in positions that require a teaching or school administrator's license, faculty of public institutions of higher education, and the educational employees of the Ohio Department of Education (Revised Code 3307.01). STRS was established in 1920.

School Employees Retirement System (SERS) — public-school employees in positions that do not require a teaching or school administrator's license, employees who provide services common to the normal daily operation of a school and are employed by private employers, and nonteaching employees of certain public institutions of higher education (R.C. 3309.01). SERS was created in 1937.

Ohio's five state retirement systems cover most state and local government employees.

There is one municipal retirement system, the Cincinnati Retirement System, and employees of state institutions of higher education have the option of participating in an alternative retirement plan instead of one of the state retirement systems.



The largest of the state retirement systems is the Public Employees Retirement System (PERS), which covers most state government employees and local government employees who are not in one of the other systems: the Ohio Police and Fire Pension Fund (OP&F), School Employees Retirement System, State Highway Patrol Retirement System, and State Teachers Retirement System.

PERS has special eligibility and benefit provisions for law enforcement officers that compare to those for members of OP&F.

Ohio Police and Fire Pension Fund (OP&F) — full-time municipal police officers and full-time firefighters employed by a fire department of the state, an instrumentality of the state, or a municipal corporation, township, joint fire district, or other political subdivision (R.C. 742.01). OP&F (formerly the Police and Firemen's Disability and Pension Fund) was created in 1967 to replace 454 local police and fire relief pension funds.

State Highway Patrol Retirement System (SHPRS) — qualified employees in the Patrol's uniform division and cadets in training. It also includes qualified employees in the radio division who were hired before November 2, 1989 (R.C. 5505.01). SHPRS was created in 1941 by the withdrawal of all state troopers from PERS.

The largest system, the **Public Employees Retirement System (PERS)**, covers state and local government employees who are not included in any of the other state retirement systems, including most state, county, and municipal employees. Employees of certain contractors that provide services formerly provided by government are also included, but only if they became members while government was performing the service. Employees of the Ohio Historical Society are specifically listed as public employees for the purpose of PERS membership. (R.C. 145.01(A).)

Certain government employees, such as election workers, are excluded

from membership (R.C. 145.012). Students employed by the schools they attend are permitted to exempt themselves from membership.² Officials in elective office are not required to become members but may choose to do so.³ PERS was created in 1935 for state employees. Local government employees were added in 1937. A program with separate retirement eligibility and benefits for law enforcement officers, such as county sheriffs and deputies and township police, was initially authorized in 1975. It is often referred to as PERS Law Enforcement Division or PERS/LE.⁴

Types of retirement plans

Background

Traditionally, public and private pension plans were established as defined benefit plans. Under such a plan, the retirement benefit is based on a predetermined formula that is not influenced by investment earnings. In recent years, many private plans have been converted to defined contribution plans, under which the earnings from investment of each participant's contributions determine the amount of the benefit. A defined benefit plan is something like an insurance program: if the appropriate contributions are made, the benefit is a readily determinable amount, regardless of how well or poorly the plan has done in investing contributions. A defined contribution



plan is more like a savings or investment program. The benefit is determined by the amount of money in the participant's account at the time of retirement.

Defined benefit plans

Under Ohio's defined benefit plans, with limited exceptions, a member receives a retirement benefit based on a formula that takes into account years of service, final average salary, and sometimes age.⁵ The plans also provide disability and survivor benefits and may include health care coverage.⁶

Defined contribution plans

Bills enacted by the 123rd General Assembly in 2000 require PERS, SERS, and STRS to create one or more defined contribution plans, in addition to their defined benefit plans.⁷

STRS — STRS has created two plans: the STRS Ohio Defined Contribution Plan and the STRS Ohio Combined Plan. Under the defined contribution plan, retirement income is based on the performance of investments that are managed by STRS and selected by the member from choices made available by STRS for investment of employee and employer contributions. There is no separate provision for disability or survivor benefits, though amounts in the account can be used for those

purposes. There is no access to retiree health care.

Under the combined plan, employee contributions are invested to fund a portion of retirement benefits in investments that are managed by STRS and selected by the member from choices made available by STRS. Employer contributions are invested by STRS to pay for retirement, disability, and survivor benefits. Access to optional health care coverage is provided to retirees who meet the necessary qualifications – currently 15 years of service credit.

PERS — PERS has also established two plans: the Member Directed Plan and the Combined Plan. The Member Directed Plan is a defined contribution plan. Under it, employee and employer contributions are deposited in the member's individual PERS account and invested as directed by the member. The benefit is based on the performance of the investment options the member selects. This plan does not include disability or survivor benefits, but the vested portion of the member's account is available in the event of disability or may be paid to survivors. A portion of the employer's contribution is accumulated in an individual retiree medical account for qualified health care expenses.

The Combined Plan differs from the Member Directed Plan in that under the Combined Plan the member directs only the investment of the

All of the state retirement systems have defined benefit plans, but in PERS and STRS certain members have the option of contributing instead to a defined contribution plan or a combined plan.

In a defined benefit plan, benefits are based on a formula that considers compensation, years of service, and sometimes age.

Defined contribution plan benefits are tied to investment returns.



employee contributions. Investment of the employer contributions is directed by PERS. Disability, survivor, and health care benefits are provided to the same extent as under the PERS defined benefit plan.

Participation — Participation in the PERS and STRS defined contribution and combined plans is limited to two groups of members: those who had less than five years of service credit on dates derived from statute and those who joined one of those systems on or after the applicable date.⁸ But even within these groups certain members are not eligible to participate. (R.C. 145.19 and 3307.25.) For both PERS and STRS, a new employee who is a “re-employed retirant” (already retired from either system or SERS) or a participant in an alternative retirement program is not eligible to participate in a defined contribution or combined plan. For STRS, a new employee is ineligible if the employee is already an STRS member participating in the defined benefit plan. For PERS, a new employee is ineligible if the employee is a PERS member with five or more years of service, a law enforcement officer, or a Hamilton County Municipal Court bailiff.

New PERS and STRS members have 180 days from the date employment begins to elect either the defined benefit plan, the defined contribution plan, or the combined plan.⁹ If no election is made, the member is deemed to have elected to

participate in the defined benefit plan. An election applies to all positions covered by the same retirement system. The statutes under which the elections are made specify that they are irrevocable; however, there are circumstances under which an election may be changed.

An STRS member who elects to participate in the defined contribution or combined plan will automatically be switched to the defined benefit plan unless the member makes an election to remain in the existing plan not later than the first day of July following the fourth anniversary of the date membership began. (R.C. 3307.88.) A PERS member in the defined contribution or combined plan can switch to the other plan or to the defined benefit plan if the plan document or rules governing the plan permit switching. (R.C. 145.814.)

Mitigating rate

Because a defined benefit plan promises to pay determinable benefits at a future time, it usually has an unfunded liability – the difference between the plan’s assets and future liabilities. The assumption is that contributions from and on behalf of current and future members will provide the assets needed to pay the promised benefits when the time comes. However, diversion of some members into a defined contribution or combined plan will affect how much is contributed to the defined benefit plan. (The issue is similar

New members of PERS and STRS have 180 days to decide which type of plan to participate in. If no election is made, the member is deemed to have elected the defined benefit plan.

Part of the employer contributions for defined contribution plan members may have to be paid to a defined benefit plan to mitigate any negative effects of the defined contribution plan.



regarding alternative retirement plans. See “*Contributions*,” below.)

To keep participation in a defined contribution or combined plan from having a negative financial impact on the PERS and STRS defined benefit plans, the Revised Code provides that a portion of the employer contributions for participants in a defined contribution or combined plan may be contributed to the defined benefit plan. (R.C. 145.87 and 3307.86.) In each case, the portion is equal to a percentage of the compensation of the members for whom the contributions are being made. This percentage is determined by an actuary appointed by the retirement board to be necessary to mitigate the negative financial impact, if any, on the system of participation in the defined benefit or combined plan. For 2008, the mitigating rate for PERS was 0.77%. For STRS, it was 3.5%.

SERS

SERS has not established a defined contribution plan. According to SERS representatives, a poll of members showed little interest, so the SERS Board decided that establishing such a plan would not be worth the considerable expense that would be involved.¹⁰

Alternative retirement plans

Establishment and membership

The faculty of the state’s public colleges and universities are generally included in the membership of STRS. Nonteaching employees are generally in PERS or, in the case of the University of Akron, SERS. Since 1997, certain of these employees have had the option of being in an alternative retirement plan (ARP) instead of a state retirement system.

Enacted in 1997, Am. Sub. House Bill 586 of the 121st General Assembly provided for the establishment of an alternative retirement program¹¹ for full-time academic and administrative employees of public institutions of higher education.¹² R.C. Chapter 3305., which was enacted by H.B. 586, requires each institution to contract with providers designated by the Ohio Department of Insurance to offer ARPs to eligible academic and administrative employees. The Revised Code provides only that each plan must be a defined contribution plan qualified under section 401(a) of the U.S. Internal Revenue Code that provides retirement and death benefits through investment options. Benefits and distributions from a plan are a matter of contract, so information about what participants will receive is available only from the plan document.¹³

Certain employees of public institutions of higher education may participate in an alternative retirement plan instead of a state retirement system.

Institutions of higher education must contract for ARPs with providers designated by the Ohio Department of Insurance.

ARPs are defined contribution plans.



A new employee of a public institution of higher education must make an election within 120 days of employment to either participate in an ARP or be a member of a state retirement system.

An eligible employee who fails to make an election is deemed to have elected to participate in a state retirement system.

Participation in an ARP was limited under H.B. 586 to two categories of full-time academic and administrative employees: those who had less than five years of service credit at the time that their employing institutions established a plan and those who were initially employed on or after the date that the plan was established. ARP eligibility was expanded in 2004 by Sub. Senate Bill 133 of the 125th General Assembly. To be eligible under S.B. 133, an existing employee had to meet all of the following conditions: (1) be a full-time employee of a public institution of higher education, (2) not have been eligible to make an election under H.B. 586, (3) as of August 1, 2005, have accrued less than five years of service credit in PERS, SERS, or STRS, and (4) have submitted notice of an election to participate in the plan not later than 120 days after S.B. 133's effective date (R.C. 3305.05).

New membership in an ARP is now open only to new full-time employees of public institutions of higher education. An election must be made in writing not later than 120 days after the starting date of employment. An eligible employee who fails to make an election within the 120-day period is deemed to have elected to participate in the applicable state retirement system. Once submitted, the election is irrevocable for as long as the employee continues to be employed by the institution. The election is

effective from the employee's starting date of employment.

An election to participate in an ARP applies to all positions at the institution unless the employee terminates employment and does not return to any position at the institution prior to one year after the date of termination.¹⁴

Providers

The board of trustees of each public institution of higher education must adopt an ARP and enter into a contract with each provider designated by the Department of Insurance that is willing to provide investment options under the plan (R.C. 3305.03 and 3305.04).¹⁵ The contract must provide for termination of the contract if the provider ceases to be a designated provider.

An employee electing to participate in an ARP must be permitted to select from among the providers that have contracted with the institution. The statute (R.C. 3305.03) requires the Department to designate at least three entities to provide investment options under ARPs, but it appears that as of November 2008 there are seven, including a number of insurance companies and TIAA-CREF, which operates retirement plans throughout the country.¹⁶ The employee must be permitted to change providers once during the first payroll period in each plan year and at any time the provider ceases to be a designated provider. (R.C. 3305.053.)



Contributions

The employee contribution to an ARP is the same as it would be to the state retirement system to which the employee would otherwise belong.¹⁷ Employee contributions are to be treated as though they were employer contributions for federal income tax purposes, which means that tax is deferred until benefits are paid. (R.C. 3305.06.)¹⁸

The employer contribution is also the same as it would be to the state retirement system to which the employee would otherwise belong, except that part of the contribution may be used to mitigate the negative financial impact of the alternative retirement program on the state retirement system. Part of the employer contribution equal to a percentage of the employee's compensation is to be paid to the applicable retirement system. The statute generally provides that the percentage is not to exceed six percent or a percentage determined by the Ohio Retirement Study Council under R.C. 171.07. However, a supplemental section provides that, notwithstanding the general provision, the percentage cannot exceed the percentage used by the applicable retirement system to mitigate the impact of its own defined contribution plans (R.C. 3305.061). The mitigating percentage is to be paid until the retirement system's

unfunded actuarial accrued liability for all benefits, other than health care and benefit increases provided after March 31, 1997, is fully amortized.

A letter to the Ohio Retirement Study Council from its actuary, Milliman USA, explained why a mitigating percentage is needed when a college or university employee chooses an ARP instead of a state retirement system.¹⁹ Each system, the letter said, relies on contributions on behalf of all employees (both current and future) to amortize the obligations that make up the system's unfunded actuarial liability. To the extent that employees choose an ARP, the financing base for amortizing the unfunded actuarial liabilities is eroded. The choice of an ARP will also affect the system's funding for retiree health care coverage. The amount set aside for health care coverage is a percentage of the employer contributions. Since, especially in STRS, college and university employees tend to have higher compensation than other state and local government employees, the amounts set aside will be higher for them than for other employees. The health care benefit is not tied to amounts contributed, and losing contributions from more highly paid members reduces the per person amount available for retiree health care.



Employee and employer contributions to an ARP are the same as to a state retirement system, but part of the employer's ARP contribution may have to be paid to the state retirement system.

The portion of the employer's ARP contribution paid to the state retirement system is intended to mitigate the negative effect of ARP participation on the retirement system.

Endnotes

¹ See “Windfall Elimination Provision,” SSA Publication No. 05-10045, January 2008, available at www.socialsecurity.gov/pubs/10045.html. See also the LSC *Members Only* brief, “Social Security Benefit Reductions Affecting Government Employees,” December 3, 2007 (Volume 127 Issue 9), available online at www.lsc.state.oh.us/membersonly/index.html.

² A member who chose as a student to be exempted may later purchase credit for the exempted services if certain conditions are met (R.C. 145.28).

³ An official in elective office or any other government employee who is not in a government retirement system is required by federal law to contribute to Social Security. To be exempt from Social Security, a person must be both a government employee and a contributor to a government retirement system.

⁴ The Revised Code does not refer to PERS/LE. Its existence can be seen only in the definitions in R.C. 145.01 and the benefit provisions in R.C.145.33.

⁵ OP&F uses the term “average annual salary.” “Final average salary” or “average annual salary” is generally the average of the member’s highest three years of compensation.

⁶ The retirement systems have authority to provide health care coverage but, with the exception of hospital coverage equivalent to Medicare A in PERS, STRS, and SERS, are not required to do so.

⁷ For STRS, the bill was Sub. S.B. 190, effective July 13, 2000; for SERS, Sub. S.B. 270, effective April 9, 2001; and for PERS, Am. Sub. H.B. 628, effective September 21, 2000. The main STRS statutes are R.C. 3307.25, 3307.251, 3307.252, and 3307.80 through 3307.89. For PERS they are R.C. 145.19, 145.191, 145.192, 145.193, and 145.80 through 145.98. For SERS, they are 3309.25, 3309.251, 3309.252, 3309.253, and 3309.80 through 3309.98.

⁸ For PERS, the date for both was December 31, 2002 (R.C. 145.191). For STRS, the date for new members was the date on which the plans were established. For members with less than five years of service, it was the thirtieth day of June immediately preceding the date on which the plan was established (R.C. 3307.25 and 3307.251).

⁹ Each system has detailed comparisons of its plans on its web site: www.opers.org and www.strs.oh.org.

¹⁰ See, Ohio Retirement Study Council, “Analysis: H.B. 320” (October 12, 2005), page 5.

¹¹ The Revised Code uses “program” to describe the overall requirement that the institutions act and “plan” for the individual plans that employees may elect.

¹² “Public institution of higher education” is defined as a state university, the Northeastern Ohio Universities College of Medicine, a university branch, technical college, state community college, community college, or municipal university (R.C. 3305.01).

¹³ In the case of PERS, an administrative rule (Ohio Administrative Code 145-1-43) requires each plan to be filed with the system, so it may be possible to get a copy of a plan document from the retirement system or the educational institution. Descriptions of the plans do not appear to be available on the Internet.

¹⁴ Shortly after H.B. 586 was enacted, there was discussion of whether those employed by contract would be permitted to make a new election with each new contract. The statute now permits a new election only if the employee is separated from employment with the institution for at least a year (R.C. 3305.05(B)).

¹⁵ To be designated a provider, an entity must meet the requirements listed in R.C. 3305.03.



¹⁶ The provider list is available on The Ohio State University's web site at <http://hr.osu.edu/benefits/retirevendors.pdf> (visited March 31, 2009).

¹⁷ For STRS and SERS, this is 10% of compensation. For PERS, it is 10% of earnable salary. "Compensation" is defined in R.C. 3307.01 and 3309.01 and "earnable salary" is defined in R.C. 145.01. Generally, both mean earnings exclusive of fringe benefits.

¹⁸ This is sometimes referred to as "employer pickup" — the contributions are "picked up" by the employer either by reducing the employee's taxable compensation or by paying the contributions in addition to the member's compensation.

¹⁹ William A. Reimert and Katherine A. Warren, Milliman USA, letter to Ohio Retirement Study Council Executive Director Aristotle L. Hutras, July 1, 2002.

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