ST. EMPLOYE RETIREMENT

GENERAL ASSEMBLY OF THE COMMONWEALTH OF PENNSYLVANIA
JOINT STATE GOVERNMENT COMMISSION
ROOM 450 - CAPITOL BUILDING
HARRISBURG 17120

MAJOR PROVISIONS OF SENATE BILL 472, P.N. 1789

ACT 31, 1974

Amendments to the State Employees Retirement Code

1. Reduction in benefit and contribution rates for legislators, judges and justices of the peace and removal of salary freeze for pension purposes effective January 1, 1973, for legislators, judges, future elected executive officers and cabinet members.

Legislators -- The benefit rate for legislative pensions is reduced to 3.462 percent and applied to a final average salary based on the actual compensation ($15,600) received. This results in the same basic dollar benefit per year of Class D-3 service ($540) as provided by existing law; however, the bill provides for a guaranteed minimum benefit equivalent to the benefit, including any cost-of-living supplements, to which a legislator would be entitled as a member of the General Assembly who retired November 30, 1970. The existing 7.5 percent benefit rate on additional compensation received as an officer of the General Assembly is continued to December 1, 1974. Thereafter, the benefit rate applied to regular compensation will also be applied to the additional compensation. Any limits on pensions attributable to Class D-3 service are retained in the event the member transfers to another class of service.

In addition, the difference between a legislator's salary and the Social Security wage base of $13,200 provides a Social Security Integration benefit of $48 per year for which he contributes $120.

Judges — The benefit rate for judicial pensions is reduced to 3 percent for each of the first 10 years of service and to 2.25 percent for each subsequent year applied to a final average salary based on the actual compensation received. For the majority of judges this provides the same dollar benefit per year of service as is provided by existing law. Again, the increases in salary would be reflected in the Social Security Integration benefits and contributions.

Justices of the Peace — The benefit rate for justices of the peace is reduced to 2.25 percent as contrasted with 3 percent under existing law.

Future Elected Executive Officers and Cabinet Members — For future elected executive officers and cabinet members who are members of the system, the benefit rate of 2 percent will be applied to their final average salary based on the actual compensation received.

2. Reduction from five to three in the number of years on which final average salary is based.

In 1972 the State Police negotiated under Act 111 to have their final average salaries based on three years. Subsequently, other employe groups and unions representing them have indicated interest in attempting to obtain such a liberalization by collective bargaining. The Federal Government and 14 other states currently base final average salaries for pensions on three-year calculations. In order to further the uniformity of benefits, the time basis used in calculating the final average salary for all employes is reduced to three years. The additional cost attributable to this change is estimated to be approximately $9 million per year initially.

3. Inclusion of employes of the Susquehanna River Basin Commission in the retirement system.

Seven employes of the commission were former state employes and retained their memberships in the retirement system. An additional 17 persons have been employed by the commission, and the commission wishes to have these employes included in the state system rather than purchase retirement benefits for them in some other manner. There is little or no cost involved to the Commonwealth, since the employer (i.e., the commission) is to pay the employer's contribution. The commission operates on an annual budget of $600,000, equally distributed among Pennsylvania, New York, Maryland and the Federal Government.

4. Optional membership for certain teachers in another approved retirement system.

Some teachers in community colleges, state colleges, etc., who have credit in national teachers' retirement systems--such as TIAA--wish to continue their memberships in these systems rather than join the state system. There is no cost to this provision since the bill provides that the Commonwealth would pay no more on account of such membership than would be paid were the teachers to become members in the state system.

5. Extension of purchase rights for multiple-service members.

This provision makes it possible to purchase previous creditable service in the state system while an active member in the school retirement system. This provision is included in anticipation of a reciprocal amendment to the school retirement code. The cost is estimated to be minimal.

6. Purchase of credit for military service.

Under this provision, all state employes--regardless of when they served in the armed forces--would be eligible to purchase up to five years of credit for military service, provided they have at least three years of state service. The cost would be based upon a person's average salary over the first three years of employment and would include interest to the date of purchase. The cost is estimated to be approximately .05 percent of payroll or $700,000 the first year.

7. Elimination of future class distinctions by permitting only Class A membership for all future employes.

Under this provision, all future legislators, judges, justices of the peace, etc., would be on the same contribution and benefit level as regular state employes. The major advantage of this proposal is the removal of the inequities of the present system of differential benefits and the possibility of substantial future cost savings.

Initially, savings would be insignificant (an estimated .018 percent of payroll or $261,000 the first year). Preliminary estimates by the actuary serving the State Employes' Retirement System indicate substantial annual savings after 10 years.

8. Elimination of distinction between voluntary and involuntary withdrawals.

Currently, members with 10 or more years of credited service who leave state employment are entitled to receive a portion of the Commonwealth's contribution to their retirement pensions if they retire involuntarily or if they arrange to be dismissed--a very common occurrence. A member leaving voluntarily receives only a return of his own contributions plus interest at 4 percent. This provision would remove this artificial distinction, and the cost is estimated to be .03 percent of payroll.

9. Termination of future Social Security Integration coverage.

The election of Social Security Integration is closed to all new entrants in the retirement system. Significant cost savings will accrue as the number of new entrants becomes substantial. The first year the savings would be small, an estimated .07 percent of payroll.

10. Termination of Social Security Integration when a member's annuity reaches his actual salary.

This amendment generally affects only those members with relatively high salaries in relation to the federal Social Security wage base. The effect would be to stop Social Security Integration contributions and the accrual of additional Social Security Integration benefits for a relatively few persons with long service at a high benefit rate, principally existing members of the judiciary. A small annual savings will result.

11. Calculation of retirement-fund liabilities on an assumption of a 5.5 percent interest rate rather than a 4.0 percent rate.

A 5.5 percent rate is more realistic in light of the current earnings rate on the fund's assets (approximately 7.0 percent) and the probability that interest rates well above 4 percent will persist for some years. A higher rate reduces the calculated future liabilities of the retirement system.

12. Limitation of pension payments to any future annuitant to the highest annual salary he received.

This is an amendment to the retirement system which has been recommended by many legislators and newspaper writers. However, the impact upon pension costs is minimal.

13. Reduction of superannuation age to 50 for correction officers and psychiatric security aides.

Approximately 2,000 members are in this group. A preliminary estimate of the cost of this provision is .057 percent of payroll.

14. Easing the limitations on earnings of disability annuitants.

Under current law, earnings permitted a disability annuitant before his annuity is reduced are limited to $5,000 or his salary at the time of disability. This provision applies a cost-of-living adjustment to the salaries at the time of disability so that the member need not give up part of his disability pension if his earning power has increased no more than the increase in the cost-of-living since his retirement. The provision also stipulates that a disability annuitant over age 50 need not report any earnings and would, therefore, receive no reduction in his annuity because of earnings. The cost of this amendment is negligible since the number of disability annuitants who have their annuities reduced because of earnings is very small--only three in the past year.

15. Provision of supplemental disability payments for members with service-connected disabilities.

Under existing law, no distinction is made between service and non-service connected disabilities for purposes of calculating disability annuities. Several employe unions have negotiated for a service-connected disability annuity of not less than 70 percent of final average salary less any Workmen's Compensation and Social Security payments received. The cost of this provision cannot be estimated because of the prior lack of distinction between service and non-service connected disabilities. However, it is not considered to be very large.

16. Expansion of Option 4 to permit a member to receive part of his retirement benefits in a lump-sum payment.

This provision would permit a retired employe to take part of his benefits, limited to the amount of his accumulated deductions, as a lump sum and receive the remainder as an annuity. This provision gives the retired employe an additional choice of options, and the only cost to the Commonwealth is a slight reduction in the earnings of the fund due to the fact that market interest rates are higher than the 4 percent statutory rate used to calculate benefits. Traditionally, the fund's actuaries have opposed lump-sum payments but have agreed that this provision, which limits the amount of such payments, constitutes no disadvantage to the fund.

17. Elimination of the reduction or loss of benefits because of death prior to superannuation age.

Under current law, the death benefit of a person who has more than 10 years of service and is either a vestee or a working member are lower than the benefits to which the person would be entitled were he to retire. It is deemed to be inequitable to continue this penalization, which was originally inserted many years ago as a cost-saving provision. The estimated cost of this liberalization of the death-benefit provision is approximately .12 percent of payroll or $1.7 million the first year.

18. Provision of a one-shot cost-of-living increase.

This provision would increase the annuities of persons who retired prior to July 1, 1967 by 30 percent and for persons who retired each year between 1967 and 1972 by an amount decreasing from 25 percent to 5 percent,respectively. The last similar cost-of-living increase was enacted in 1967. The cost of this proposal--the most costly of all the provisions under consideration--is about $8 million, terminating in about 20 years.

19. Establishment of an independent retirement board and increasing the board membership from five to seven.

Under this provision, the retirement board would be removed from its status as a departmental board in the Department of State and made administratively independent. The bill provides that six of the members of the board be appointed by the Governor and confirmed by the Senate. The proponents of this change view this as increasing the flexibility of the board both in administration and composition and guaranteeing adequate representation on the board via the Senate confirmation.

20. Requiring the retirement board to submit an annual budget to the General Assembly.

Currently, the retirement board finances its administrative expenditures from earnings of the fund in excess of statutory interest and does not receive an appropriation from the General Assembly for these expenses. This provision, by requiring the board to submit a budget and receive direct approval for its expenditures through an appropriation act, would give the General Assembly greater knowledge and direction over the independent board's operations than it now has over the board as a departmental component of the Department of State. In addition to the advantage of greater legislative supervision, this provision is considered to be necessary to implement the constitutional requirement that all public expenditures be included in the Governor's budget submitted to the General Assembly.

21. Actuarial determinations of employer contribution rates to be considered as final.

In the past, actuarial recommendations as to the appropriate employer contribution rate have often been reduced by the Governor's budget officials, resulting in lower appropriations to the retirement fund than the actuary deemed necessary. The proposed change should tend to reduce such deficit-increasing practices in the future.

22. Assignment of rights to certain credit unions.

These rights are provided for in current law but were eliminated in the original draft of Senate Bill 472 as being burdensome to the retirement board and creating a small additional cost to the Commonwealth. The rights were restored by the Senate Finance Committee since many state employes felt that this privilege should be continued.

23. Restriction of future collective bargaining by state employe unions for retirement benefits.

Without this amendment, the practice of various employe unions bargaining for additional retirement benefits could be expected to grow, with the possibility of a serious long-term impact upon the solvency of the fund as has been the experience in other states.

24. Discontinuance of special retirement benefits for judges age 70 and over.

This proposal removes from existing law the provision which permits judges age 70 and over to "retire" on full salary until the end of their terms. Thereafter, they may receive regular retirement benefits according to their service records. Since the constitutional amendments of 1968 prohibit judges from serving past the age of 70, this provision is not only contradictory but obsolete. The change does not affect judges who have already chosen this benefit.

25. Investments

This amendment provides that the allowable book value investment in common stock be increased from 10 percent to 25 percent of the total assets of the fund. It deletes the restriction that the total amount invested in common stocks at any time shall not exceed 50 percent of the total amount of the fund invested in mortgage loans on real estate located in the Commonwealth of Pennsylvania which are insured by the Federal Housing Administration or the Veterans' Administration.

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Cost estimates in the above discussion reflect the anticipated payroll in 1974-1975 ($1.45 billion). Some of the earlier estimates were based on the 1972-1973 payroll ($1 billion), and the original cost estimate for the purchase of military credit was based on the 1971-1972 payroll ($840 million).

STATE EMPLOYES' RETIREMENT SYSTEM OF PENNSYLVANIA

COSTS OF SENATE BILL NO. 472 (PRINTER'S NO. 1789)
BASED ON COVERED PAYROLL OF $1,450,000,000

Section	Item	Total	First Year Cost
STATE ANNUITY ACCUMULATION ACCOUNT			
Additional Costs (Annual)			
5102	3-year final average salary.................	.652%	$ 9,454,000
5102	Superannuation retirement Age 50 - correction officers	.057	827,000
5102	Flat 5% regular member rate........:.....	Minor	
5304	Military service...........................	.050	725,000
5308	Early annuity 10 years.....................	.030	435,000
5704	Disability benefits........................	.010	145,000
5707	Death benefits - actives and vestees.......	.120	1,740,000
	Gross annual additional costs.......................	0.919%	$13,326,000
Annual Savings			
5306	New members Class A only...................	.018%*	$ 261,000*
5504	4% interest on back contributions..........	.040	580,000
5706	Actuarial adjustment-on second retirement...	.020	290,000
-	Elimination of special retirement benefits for judges......................	.020	290,000
-	Discontinuation of SSI elections...........	.070**	1,015,000**
	Total annual savings.............................	0.168%	$ 2,436,000
	Net annual additional costs.............................	0.751%	$10,890,000
SUPPLEMENTAL RETIREMENT ALLOWANCE ACCOUNT			
Additional Costs (Annual)			
5708	Cost-of-living increases..................	0.551%	$ 8,000,000
TOTAL ADDITIONAL ANNUAL COSTS	....	1.302%	$18,890,000

*Estimated to increase to approximately 0.18% of payroll in 20 years. Assuming future salary increases at 4% annually, this would amount to an annual saving then of approximately $5,720,000. Consequently, the average annual saving during this period would approximate $3,000,000.

**Estimated to increase to 0.70% of payroll in 20 years, or approximately $22,250,000 annually assuming future salary increases at 4% annually. The average annual saving during the 20-year period would approximate $11,600,000.