



Commission on Government Forecasting and Accountability

PENSION IMPACT NOTE *103RD General Assembly*

BILL NO: **HB 3270**

February 21, 2023

SPONSOR (S): Weaver

SYSTEM: General Provisions Article (SERS, SURS, and TRS)

FISCAL IMPACT

The fiscal impact of implementing the Tier 3 system has not been calculated by the Big 3 State Systems (SERS, TRS, and SURS). Inasmuch as the plan has not been implemented, no actuarial assumptions have been developed by the State system actuaries as to the number of Tier 2 members who would opt in to the Tier 3 plan. Please see Appendix I on Page 3 of this note for a summation from SURS on the issues that would need to be resolved before Tier 3 can be properly implemented.

SUBJECT MATTER: HB 3270 amends the General Provisions Article of the Pension Code to mandate that the Big 3 State Systems (SERS, TRS, and SURS) set an Implementation Date for the Tier 3 plan of July 1, 2025.

COMMENT: P.A. 100-0023, which took effect on July 6th, 2017, created a “Tier 3” plan for the Big 3 State Systems (SERS, SURS, and TRS; only SERS members who are not coordinated with Social Security can participate in Tier 3). The Tier 3 plan had no impact upon Tier 1 members, but it gave Tier 2 members the option of joining the Tier 3 plan. After Tier 3 is implemented (a date known in statute as the “Implementation Date”), newly-hired members will automatically be enrolled into the Tier 3 plan unless they opt into Tier 2. Tier 3 is a hybrid retirement plan that consists of 2 parts – a small defined benefit (DB) plan, and a defined contribution (DC) plan.

Below is a summary of the benefit features of the Tier 3 plan:

- Members will contribute a minimum of 4% to the DC portion of the plan and 6.2% towards the DB portion of the plan, but the employee DB contribution shall not

exceed the employer's normal cost of the DC plan. If the employer's normal cost is less than 6.2% of payroll, then the employee contribution to the DB component shall be lowered to match the employer's normal cost. Employer matching contributions to the DC plan will be no less than 2% of salary and no higher than 6% of salary;

- Normal retirement age for the DB portion of the plan is determined by the Social Security retirement age, which is currently 67 years of age;
- The Final Average Salary (FAS) for calculating an initial DB pension is the member's average annual salary during the last 10 years of service;
- The DB automatic annual increase (AAI) is similar to the Tier 2 AAI – one-half of the previous year's consumer price index, not compounded;
- The Tier 3 calculation for an initial pension is years of service multiplied by Final Average Salary multiplied by 1.25 percent;

The State Systems have not, as yet, implemented the Tier 3 plan. P.A. 100-0023 granted the power to each respective system's board of trustees to set the Implementation Date. HB 3270 mandates that TRS, SERS, and SURS must implement Tier 3 no later than July 1, 2025.

Please see Appendix I on the following page for an explanation from SURS on the issues that need to be resolved before Tier 3 can be implemented.

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Appendix I

Below is a summary provided by SURS of the issues that would need to be resolved before the Tier 3 hybrid plan can be properly implemented:

- SURS needs to implement a number of DC plans to comply with the benefits of the law; however, only 401(a) plans are “qualified plans;”
- The IRS prohibits elective deferrals, so a solution needs to be addressed for the minimum employee contributions to the DC portion of the plan;
- The IRS may have concerns with existing Tier 2 employees being afforded the opportunity to change their employee contribution rates (i.e., switching from 8% to 6.2%) under the DB portion of the Optional Hybrid Plan;
- The requirement to use ISBI’s investment options under the DC portion of the Optional Hybrid Plan should be stricken;
- The Optional Hybrid Plan election period should be consistent with SURS’ plan election period for new members;
- SURS needs to know which contribution rates to charge employees and employers until the employees make a plan election;
- There should be consistency in the timing of automatic annual increases under the Optional Hybrid Plan and Tier 2;
- SURS needs language to collect contributions from employers whose employees are paid from trust funds, state grants, and federal funds;
- SURS needs guidance from the General Assembly on:
 - o How to calculate benefits for Tier 2 members who elect to participate in the Optional Hybrid Plan – There are several questions on this topic;
 - o How to calculate the final average salary to perform benefit calculations;
 - o Whether the minimum retirement and minimum survivor benefits apply to participants in the Optional Hybrid Plan;
 - o How to split DB contributions for the purposes of calculating refunds under the Optional Hybrid Plan;
 - o How to administer service credit purchases under the Optional Hybrid Plan; and
 - o How to administer return to work provisions under the Optional Hybrid Plan.