

# Retiree Benefits in Public Pension Systems

## Select Committee on Pension Policy

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<http://www.wsipp.wa.gov/rptfiles/12-12-4101r.pdf>

Background

State Plans

Portability

Overtime

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## Study Assignment

*“conduct an evaluation of the benefits provided in the pension plans offered by public employers in the state”*

- Compare benefit levels across public retirement plans.
- Identify barriers to portability of retirement benefits among public employers in the state.
- Describe how “excess compensation” (including overtime) is handled in pension calculations.

*Supplemental Operating Budget § 606 (13), 2012 Wash. Sess. Laws 2225*

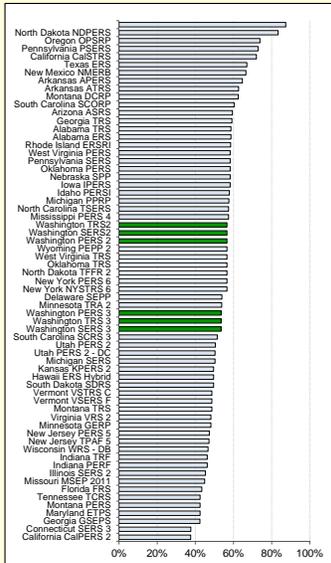
## Comparing Benefit Levels Across State Plans

- “Income replacement” measure
- General and teacher-type plans (n = 65)
- Police and fire fighter-type plans (n = 43)
- Most recent open plans
- Allow contributions to Social Security
- Two hypothetical retirees
  - ✓ Age 65, 30 years of service
  - ✓ Age 55, 30 years of service
  - ✓ Salary history estimated with Washington DRS data

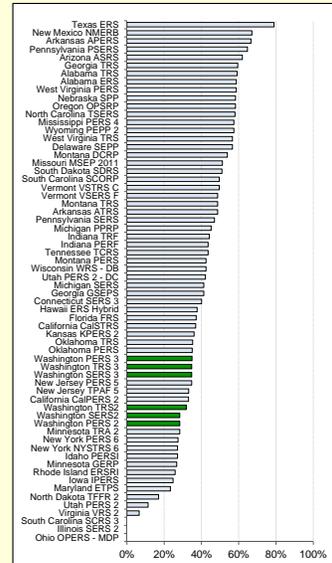
### Comparing Benefit Levels Across State Plans

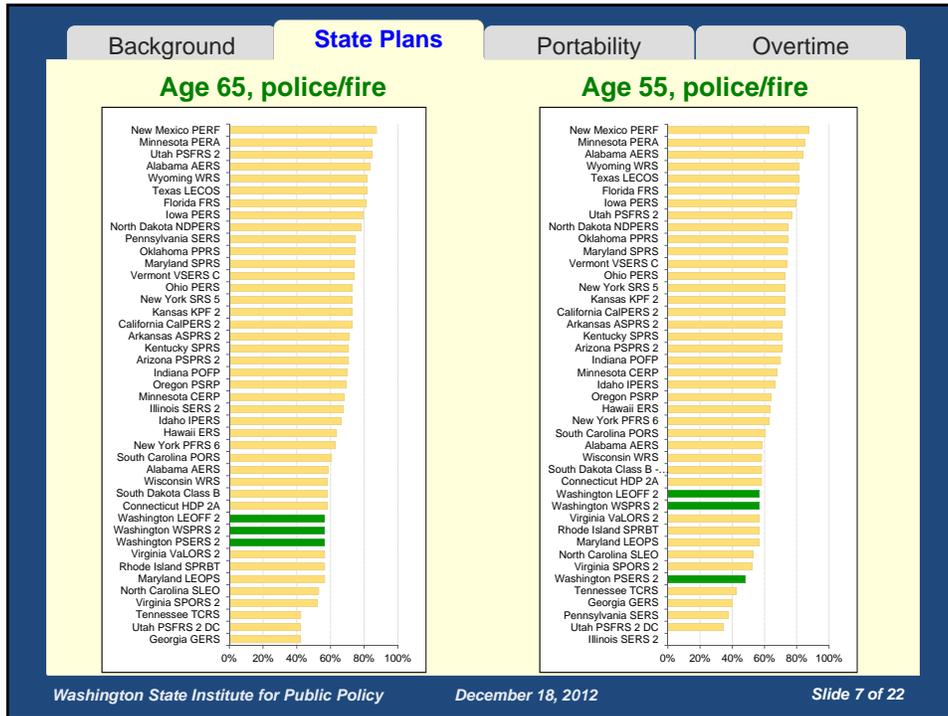
- Assumptions:
  - ✓ Default contribution rates
  - ✓ Median benefit multipliers
  - ✓ Growth and distribution of DC benefits
- Limitations:
  - ✓ Measure does not include Social Security, private savings/investments, COLA, health benefits
  - ✓ Assumptions about annuity purchases may not reflect actual behavior

### Age 65, general/teacher



### Age 55, general/teacher





Background State Plans **Portability** Overtime

## Local Public Pensions in Washington

- Most local governments participate in state plans.
- Exceptions:
  - ✓ Seattle
  - ✓ Spokane
  - ✓ Tacoma
  - ✓ Lakewood
  - ✓ Sound Transit

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## Tradeoffs: Stability and Mobility

	Defined Benefit Plan	Defined Contribution Plan
<b>Benefit determined by</b>	Salary & years of service	Contributions & investment returns
<b>Predictability</b>	Very predictable	Less predictable
<b>Portability</b>	Less portable	More portable
<b>Advantages for</b>	Long job tenure	Mobile workers

Hybrid plans (Plans 3) contain elements of both.

## Washington State Portability Laws & Rules

- Dual membership:
  - ✓ Combine service credit across jobs for eligibility
  - ✓ Use highest salary across jobs
  - ✓ Purchase service credit
- An option for most state plans and Seattle, Spokane, Tacoma
- Does not apply to Lakewood, Sound Transit, other DC plans

## Overtime and Excess Compensation Data

### Department of Retirement Systems (DRS) data

- Members retiring from state plans 1/2009 to 6/2012:
  - ✓ Demographics, employer, pension plan, retirement date, average final compensation (AFC), cash-outs, excess comp.
  - ✓ Earnings history: compensation and hours worked up to ten years prior to retirement.
- Limitations – overtime hours and earnings not reported separately; no indication if mandatory or voluntary

### Human Resource Management System (HRMS) data

- Information on overtime compensation
- Covers state agency employees
- Data begin July 2006

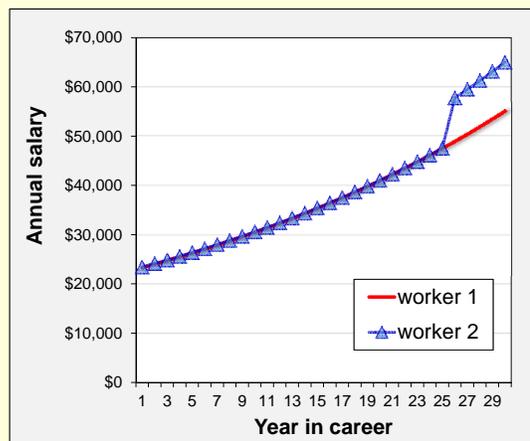
## Stylized Example 1: End-of-Career Increases

**Worker 1:** no overtime

**Worker 2:** no overtime until last 5 years of career, then 20 hours/month

**For Worker 2:**

- ✓ Pension benefits higher than anticipated
- ✓ Contributions cover a small portion of costs



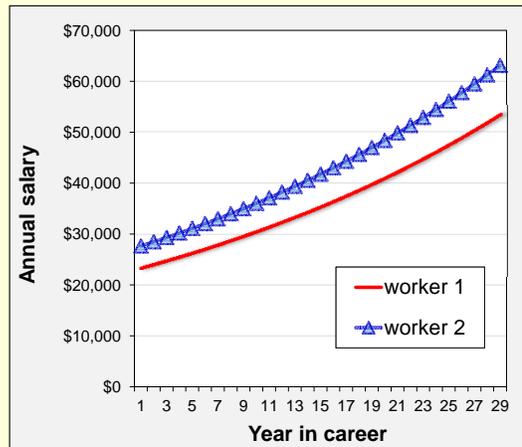
## Stylized Example 2: Higher Hours Throughout Career

**Worker 1:** no overtime

**Worker 2:** consistent overtime hours throughout the career

**For Worker 2:**

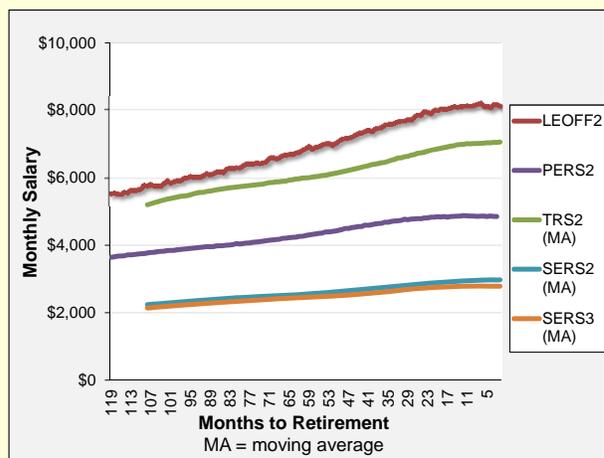
- ✓ Pension benefits higher as expected
- ✓ Worker and employer contributions cover the costs



## Average Earnings

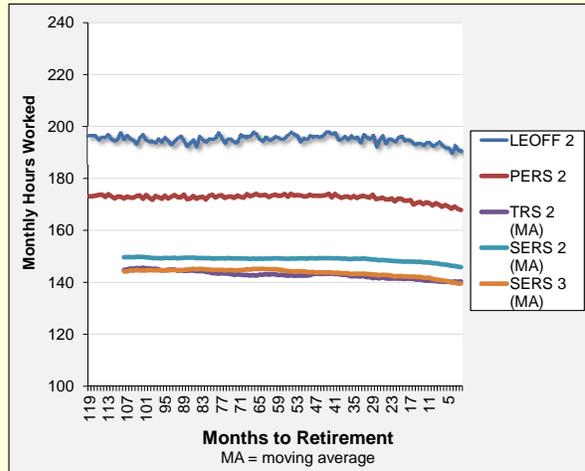
- ✓ Earnings rise with tenure for several reasons
- ✓ These increases impact AFC levels
- ✓ Seniority-based pay systems have advantages

*Average Earnings Profiles for Washington Open Public Plans, Retirements from January 2009 to June 2012*



## Average Hours

- ✓ Higher earnings/hour, not hours worked, typically drive earnings growth
- ✓ Avg. monthly hours not systematically higher during AFC periods
- ✓ Average hours across plans and employer groups vary widely



Average Hours Profiles for Washington Open Public Plans, Retirements from January 2009 to June 2012

## Average Hours Before & During AFC Period

System/ Plan	N	Avg. Hrs Pre- AFC	Avg. Hours AFC	Difference	Std Dev AFC Avg.
LEOFF1	109	186.3	182.9	-3.40	21.8
LEOFF2	731	195.4	194.9	-0.50	26.1
PERS1	3,577	170.2	169.3	-0.90	18.8
PERS2	6,182	173.0	172.1	-0.90	17.8
PERS3	158	171.1	169.0	-2.10	20.1
SERS2	1,115	147.2	146.1	-1.10	28.0
SERS3	251	143.0	140.8	-2.20	26.9
TRS1	1,968	153.1	154.1	1.00	18.7
TRS2	558	143.6	141.3	-2.30	14.1
TRS3	258	141.0	139.1	-1.90	18.3
WSPRS1	99	180.3	177.2	-3.10	9.7

## Variation in Hours Increases

- ✓ Across all systems, roughly 3% of retirees worked 20 or more additional hours per month during AFC periods than before.

### Difference in Average Monthly Hours: All Systems and Plans

Average Hours Worked Gain/Loss Pre- and Post-AFC	Retirees	Percent
Less by > 2 hours	4,631	30.9%
Near, -2 to <2 hours	6,957	46.4%
More, 2 to <10	2,305	15.4%
More 10 to <20	698	4.7%
More, 20+	415	2.8%

## Variation in Hours Increases

- ✓ Most work roughly the same hours before and during the AFC period.
- ✓ Those who work overtime at the end of their career tended to do so earlier.
- ✓ There are exceptions; extreme increases in hours are rare.
- ✓ Hours decline for some members.

### Retirees by Average Hours Before and During AFC Period: All Systems & Plans

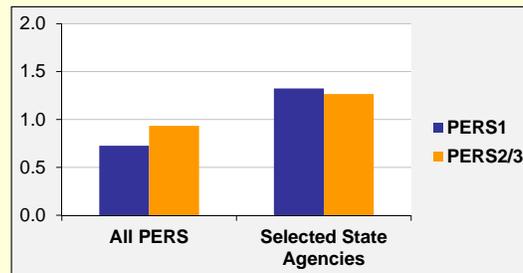
Average Hours: Pre-AFC	Average Monthly Hours: AFC Period						
	(1) <128 (15-29/wk)	(2) 128-149 (30-34/wk)	(3) 150-166 (35-38/wk)	(4) 167-179 (39-41/wk)	(5) 180-192 (42-45/wk)	(6) 193-214 (45-49/wk)	(7) 215+ (50+/wk)
(1) <128 (15-29/wk)	699	131	35	20	3	0	1
(2) 128-149 (30-34/wk)	240	1153	382	65	11	7	2
(3) 150-166 (35-38/wk)	47	470	1189	369	32	5	9
(4) 167-179 (39-41/wk)	29	107	413	7151	357	34	13
(5) 180-192 (42-45/wk)	0	6	37	543	577	134	16
(6) 193-214 (45-49/wk)	1	2	4	59	137	236	50
(7) 215+ (50+/wk)	0	0	0	14	15	36	165

## Response to Pension Incentives?

Natural Experiment

- ✓ Different incentives 5 to 3 years before retirement for PERS1,2/3
- ✓ Incentive effect measured by difference in additional hours by plan
- ✓ Regression estimates for all PERS and selected (higher OT) state agencies
- ✓ Some (not robust) evidence for a modest incentive impact

Estimated Additional Hours Per Month During AFC Period, On Average



## HRMS Overtime Compensation Data

Matched data for a sample of state agency retirees in the study

### Average Annual Overtime (OT) Compensation

Sample of State Agency Retirees	Average OT Pay	OT Share of Annual Compensation
All Retirees, including OT=0	\$735	1.26%
Retirees with OT>0	\$2,670	4.60%

### Distribution of Overtime (OT) Compensation (among cases where OT>0)

OT Range from to	Annual Observations	%
\$1 < \$100	168	10.6%
\$100 < \$500	330	20.8%
\$500 < \$1000	209	13.2%
\$1,000 < \$2500	395	24.9%
\$2,500 < \$5000	273	17.2%
\$5,000 < \$10,000	130	8.2%
\$10,000+	83	5.2%
Total	1,588	100.0%

## State Policies on Pensions and Overtime

- “Excess compensation” charges: WA, IL
- Limit AFC as % of final salary or as a \$ amount (less than half of states)
- Set longer AFC period (FL, IL at 8 years)
- Exclude overtime from AFC (28 states)
- Exclude leave cash-outs from AFC (about half of states)

*AFC = average final compensation*

## Questions?