

Consideration of changing new employee’s retirement plan from defined benefit to hybrid defined benefit/defined contribution

GOAL: To determine and recommend that Roane County either maintain all new employees on the defined benefit plan or propose the new employees be placed under the hybrid plan.

OBJECTIVE: To analyze and document the advantages and disadvantages of both retirement plans from the employer and employee’s perspectives.

FACTS:

1. Current Tennessee Consolidated Retirement System (TCRS) is a defined benefit plan which historically has an actuarial study completed every two (2) years that establishes the employer contribution rate.
2. Roane County teachers are considered state employees for retirement purposes and new teachers were placed under the new hybrid plan effective July 1, 2014.
3. Local municipalities (counties and cities) have the option for new employees to be covered under the existing plan, a new hybrid plan or other alternate retirement plans provided for within the law.
4. Of the available retirement plans through TCRS, our analysis focuses on the current plan and the hybrid plan that is currently in place for state employees and teachers.
5. School classified employees (non-teachers), county general, highway and other county department employees are considered municipality employees.
6. Resolution to change to the hybrid system upon adoption would take effect six (6) months after resolution approval.
7. Current defined benefits accrual rate is adjusted every two (2) years with an anticipated implementation taking place every year beginning next year.
8. Current defined benefit fact as provided in the June 30, 2013 Annual Financial Report are:
 - Employees contribute 5% of their earnings toward a defined benefit plan
 - The county contributes 9.14% of annual covered payroll toward a defined benefit plan
 - Annual Pension cost to the county of \$1,563,183 paid into TCRS
 - Rate is based on return on investment (ROI) of 7.5%, 3% annual rate of inflation, projected salary increases of 4.75% (graded), 3.5% growth in the Social Security wage base, projected postretirement increases of 2.5%
 - TCRS in sum is funded at 98.31%
9. Comparison of the two retirement rates plans:

	Defined Benefit	Hybrid	
		Defined Benefit	Defined Contribution
Employee	5%	5%	2% unless opt out
Employer	8.45% adjustable	5%	4%

10. TCRS defined benefit plan actuarial study provides the new employer's rates to support anticipated pay outs based on life expectancy, investment performance, current employee payment into the system and other factors that are subject to annual changes. TCRS employer rate will change.
11. The hybrid system establishes the employer contribution at 9% with any change in the defined benefit rate being adjusted within the 9% between defined benefit and defined contribution.

ANALYSIS:

Following is an analysis as if the hybrid plan had been in place for the last four (4) rate changes. The county 401(k) matching program did not start until 2012 for consistency purposes we have included these expenses as if they had been going on in prior years.

	Contribution		Cost of	Cost of	Total	% with	Difference
	Rate	Payroll	TCRS	401(k) match	Retirement	401 (k) match	to Hybrid Plan
Rate 2008/2009	7.86%	10,168,320	799,230	72,930	872,160	8.58%	42,989
Rate 2009/2010	7.84%	10,168,320	797,196	72,930	870,126	8.56%	45,023
Rate 2010/2011	9.05%	10,168,320	920,233	72,930	993,163	9.77%	(78,014)
Rate 2012/2013	9.14%	10,168,320	929,384	72,930	1,002,314	9.86%	(87,166)
Rate 2014/2015	8.45%	10,168,320	859,223	72,930	932,153	9.17%	(17,004)
Average	8.47%	10,168,320	861,053	72,930	933,983	9.19%	(18,835)
Hybrid	9%	10,168,320	915,149	incl.	915,149		-

The current contribution rate of Roane County is 8.45% which is a variable rate adjusted every two (2) years. It is our understanding that TCRS is changing their actuarial time and will be making these adjustments each year. Below is an example of potential rate changes based on previous rate changes and estimated potential changes.

Change in Cost of Old TCRS should the rate change				
<u>Current Rate</u>			<u>Potential Rate</u>	<u>Cost Difference</u>
8.45%	-0.69%	+	7.76%	(70,161)
8.45%	-0.02%	+	8.43%	(2,034)
8.45%	0.09%	+	8.54%	9,151
8.45%	0.80%	*	9.25%	81,347
8.45%	1.05%	*	9.50%	106,767
8.45%	1.21%	+	9.66%	123,037
8.45%	1.55%	*	10.00%	157,609

* Shows potential rate growth
 + shows past rate increases/decreases as applied to current rate

Below is an example of the cost difference to the county as if the hybrid plan were adopted and it was applied to \$600,000 of new employees salaries and the current contribution rate for the county remained the same for old employees. These hypothetical new employees would be those hired six (6) months after the approval of a resolution to change the retirement system. With our current rate (excluding the current county 401(k) match) it would be more expensive to move to the hybrid plan. If this salary represents 20 employees who all take the county 401(k) match that adds \$9,600 of county expense to the “total on old plan “ line.

As if \$600,000 of old employees were replaced with new employees on the hybrid plan	
Salary (old)	\$ 9,568,320
Rate	<u>8.45%</u>
Cost of TCRS	\$ 808,523
Salary (new)	\$ 600,000
Rate	<u>9.00%</u>
Cost of TCRs	\$ 54,000
Old Emp	\$ 808,523
New Hybrid	<u>\$ 54,000</u>
Total	\$ 862,523
Total on Old Plan	<u>\$ 861,053</u>
Difference	\$ (1,470)

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As if old rate increased and \$600,000 of old employees were replaced with new employees on the hybrid plan		
Salary (old)	\$	9,568,320
Rate		<u>9.25%</u>
Cost of TCRS	\$	885,070
Salary (new)	\$	600,000
Rate		<u>9.00%</u>
Cost of TCRS	\$	54,000
Old Emp	\$	885,070
New Hybrid	\$	<u>54,000</u>
Total	\$	939,070
Total on Old Plan	\$	<u>940,570</u>
Difference	\$	1,500

Employee 401(k)

The hybrid plan funds a 401(k) which allows the employees to take their retirement (entire 401(k) portion) with them should they sever employment. The current TCRS program allows employees only to take their own investment and not the county’s investment in their retirement. The 401(k) portion allows the employee to take both portions of their retirement with them when they leave. The employees are still entitled to the portion they have contributed to the defined benefit portion as well. The shaded portions of each plan show the contribution that can be received after a vesting period of five (5) years. The unshaded portion has no vesting requirements.

	Defined Benefit	Hybrid	
		Defined Benefit	Defined Contribution
Employee	5%	5%	2% unless opt out
Employer	8.45% adjustable	5%	4%

RECOMMENDATION: The Roane County Executive’s office sees no significant financial support of savings or expense between the programs initially. The benefit lies in the potential rate changes made by TCRS in each consecutive year. Additionally the hybrid provides stability in budget planning with a constant rate of 9%. Should the County Legislative Body choose to adopt the new hybrid retirement system for all new employees then those new employees should be exempted from the current 401(k) match program in effect which is at the set rate of \$480 per year.

Additional information about all of the plans available is located at <http://www.treasury.state.tn.us/tcrs/>

Executive Summary #42 is on the website.