

PUBLIC EMPLOYEE RETIREMENT COMMISSION

ACTUARIAL NOTE TRANSMITTAL

Bill ID: Senate Bill Number 25, Printer's Number 20
System: Public School Employees' Retirement System
Subject: Purchase of Service Credit for Unused Sick Leave

SYNOPSIS

Senate Bill Number 25, Printer's Number 20, would amend the Public School Employees' Retirement Code to permit an active member or active multiple service member of the Public School Employees' Retirement System (PSERS) to purchase school service credit for unused sick leave accumulated prior to the member's effective date of retirement. Under the bill, a member would be permitted to purchase the service credit at the time of filing an application for retirement and would receive school service credited as Class T-C. The bill mandates that the contributions required to purchase the Class T-C service credit for creditable sick leave will be the sum of the member's basic contribution rate and the employer normal contribution rate at the time the creditable sick leave is purchased based on the member's per diem salary for the year in which the service is purchased.

DISCUSSION

The Public School Employees' Retirement Code (Code) is a governmental, cost-sharing, multiple-employer pension plan. The designated purpose of the Public School Employees' Retirement System (PSERS) is to provide retirement allowances and other benefits, including disability and death benefits, to public school employees. As of June 30, 2002, there were approximately 695 participating units, generally school districts, area vocational-technical schools, charter schools, and intermediate units in PSERS. Membership in PSERS is mandatory for most public school employees. Certain other employees are given the option to participate. As of June 30, 2002, there were 242,616 active members and 141,414 annuitant members of PSERS.

Under the Code, members may retire at age 60 with 30 years of service credit, age 62 with one year of service credit, or at any age with 35 years of service credit. Generally, the retirement benefit is the product of 2.5 percent multiplied by the number of years of service credit multiplied by the member's final average (highest three years) salary. The number of years of credited service have a direct impact on the benefit amount for both regular and early

DISCUSSION (CONT'D)

retirement. Public employee defined benefit pension plan provisions that permit members to receive additional service credit without actually rendering service to the public employer are of value to the members because they enhance the retirement benefit and also may accelerate eligibility for retirement and certain ancillary benefits related to retirement (such as eligibility for postretirement health care benefits).

In computing the credited school service of an active member of PSERS for the determination of benefits under Section 8302 of the Code, a full-time salaried school employee is credited with one year of credit for each school year, or corresponding fraction of a year, in accordance with the proportion of the full school year for which the required member contributions have been made. A per diem or hourly school employee receives one year of credited service for each nonoverlapping period of 12 consecutive months of employment, and for which required contributions are made, for at least 180 full-day sessions or 1,100 hours of employment. If a member is employed and contributions are made for less than 180 days or 1,100 hours of employment, the member receives credit for a fractional portion of a year. Members may also receive credited school service for approved leaves of absence and for periods of activated military service.

The bill would amend the Code by permitting school employees to purchase credited school service for any unused sick leave accrued by the member prior to retirement. The effect of the additional service credit would be to add to the value of the basic retirement benefit prior to modification and may accelerate retirement eligibility.

Currently, school employees are permitted to receive payment for all or a portion of the value of their accumulated sick and annual leave at retirement. The exact nature of these leave "payouts" varies according to the personnel and leave policies of the individual school employer. The bill would permit a member to continue to receive sick leave payouts from the school employer at retirement and also receive retirement service credit in PSERS for the same unused sick leave.

Due in part to the decentralized nature of public school employment in the Commonwealth, the nature of the collective bargaining process and the resulting wide variation in contractual agreements among the more than 500 public school districts and nearly 200 other school employers that participate in PSERS, the Commission staff was unable to obtain reliable data on the sick leave accumulation rates and leave payout policies of school employers. The Commission staff was able to obtain a 1991 study by the Pennsylvania School Boards Association entitled "Teacher Absenteeism: Professional Staff Absence Study - School Year

DISCUSSION (CONT'D)

1990-91.” A review of this study and related materials revealed that: 1) the public School Code of 1949 mandates that public school employees be permitted a minimum of 10 days of sick leave per year, although school employers may, and generally do, provide for more liberal sick leave allocations; and 2) on average, teachers used 5.5 days of sick leave per year, including sick family days. These data would suggest that public school employees will on average accrue a minimum of 4.5 days of unused sick leave per year over the course of their careers. Based upon a 180-day year, and an average career length of 23.88 years, members would be eligible to purchase service credit for at least an additional 0.60 years of school service.

Under the bill, the member’s contribution required to purchase the additional school service credit would be the sum of the member’s basic contribution rate and the normal contribution rate at the time the creditable sick leave is purchased based upon the member’s per diem salary for the year in which the service is purchased. The bill provides for the crediting of the purchasable sick leave as Class T-C only and makes no provision for the crediting of the service as Class T-D (membership in which provides a benefit enhancement of 25% over Class T-C service), despite the fact that most members of PSERS have elected membership in Class T-D. Therefore, the bill appears to require the member to pay for the additional service credit at the higher Class T-D contribution rate while providing only Class T-C service credit. It is unclear whether this is the intent of the bill sponsors or is merely a drafting error. Finally, the employer normal contribution rate, which is a factor in the purchase amount, also reflects the cost of Class T-D service rather than Class T-C service.

SUMMARY OF ACTUARIAL COST IMPACT

Based upon information received from the Public School Employees’ Retirement System, the Pennsylvania School Boards Association and other sources, the Commission requested its consulting actuary to assume that each member would accumulate a minimum of 4.5 days of unused sick leave per year over an average career length of 23.88 years. The Commission’s consulting actuary also assumed that 9,900 members would retire each year, an average member salary of \$45,000, an employer normal contribution rate of 7.25%, and that all eligible members would elect to purchase the school service credit for their unused sick leave.

SUMMARY OF ACTUARIAL COST IMPACT (CONT'D)

Based on these assumptions, the consulting actuary of the Commission determined that the service purchase authorization provided under the bill would have the following costs.

	Amount	
First Year Increase in Unfunded Actuarial Accrued Liability ¹	\$25,000,000	
	Amount	As a % of Payroll
Increase in Employer Annual Costs ³		
First Year Increase in Amortization Payment ¹	\$ 4,100,000	.04%
Projected Increase in Amortization Payment ²	\$65,695,000	.35%

¹ The unfunded actuarial liability will increase annually by \$25,000,000. For each day that the per member average accumulated sick leave is increased, \$5 million is added to the estimated annual increase in the unfunded actuarial accrued liability.

² Approximate increase in amortization payment after ten years.

³ Paid in part by the Commonwealth and in part by the school districts and other educational employers.

POLICY CONSIDERATIONS

In reviewing the bill, the Commission identified the following policy considerations:

Departure from Policy Guidelines. In March of 1997, the Public Employee Retirement Commission published *Service Purchase Authorizations for Pennsylvania Public Employee Retirement Systems*, a report recommending policy guidelines for authorizing, funding, and structuring service purchases. The bill does not conform to recommendations in the report concerned with authorizing, funding, and structuring service purchases.

POLICY CONSIDERATIONS (CONT'D)

Appropriateness of Service Credit for Unused Sick Leave. (-) The specific situations for which the Commission considered the use of service purchase authorizations to be appropriate were limited to those involving military service, transfers of governmental function, the reinstatement of service credits following a break in service, and remedying inequalities caused by employer actions. Currently, as a matter of personnel policy, school employees are permitted to receive cash payouts at retirement for periods of unused sick leave and for other types of accumulated, unused leave, but no provisions are made in the PSERS Code to permit school service credit for such periods of unused sick leave. The bill would expand the service credit provisions of the Code to include periods of unused sick leave, a type of service credit not among those recommended by the Commission.

Adequacy of Purchase Payments. (-) The method for calculating the member contributions to purchase service credit for school service proposed in the bill will result in the member paying less than the full actuarial cost of the increased benefit acquired through the service credit purchase. This service credit purchase price will result in an increase in the unfunded actuarial accrued liability of PSERS and in increased amortization payments.

Cost Effective Technical Provisions. (-) For service purchase authorizations of this type, the Commission recommended that, in cases where the service purchase amount required to be paid by an employee includes amounts representing both employer and employee costs attributable to the purchased service, the portion of the payment representing employer cost be precluded from withdrawal by a member upon retirement. The bill contains no prohibition from withdrawal of the service purchase amount under retirement Option 4.

Disparity in Benefit Between SERS and PSERS. () The bill proposes to permit purchases of service credit for periods of unused sick leave by members of PSERS and not members of the State Employees' Retirement System (SERS). This approach is a departure from the General Assembly's long-standing practice of providing substantially identical benefits to members of both statewide systems.

POLICY CONSIDERATIONS (CONT'D)

Potential for Abuse. (-) It is possible that permitting members to purchase service credit for unused sick leave could stimulate a change in personnel policy on the part of school employers, whereby school employers could offer excessively liberal sick leave accrual policies while eliminating or restricting sick leave cash payouts. This would have the effect of shifting the costs associated with sick leave policies from the school employer to PSERS.

Redundant Service Credit. (-) The proposal would result in members receiving double service credit for the service time represented by the unused sick leave.

Drafting Ambiguities. () In reviewing the bill, the Commission staff noted the following drafting ambiguities.

Class T-C Service Credit for School Service. The bill appears to require payment of Class T-D member contributions (6.5% or 7.5%) while crediting members with Class T-C (member contribution rate of either 5.25 or 6.25) service credit. It is unclear whether this provision was the intent of the bill sponsors or a drafting error.

Administrative Reporting Requirements. Normally, school employers are required to report to PSERS any information that would impact the retirement benefits of members. The bill should be amended to require school employers to regularly report unused accumulated sick leave of employees to PSERS, since this information could impact the calculation of the member's retirement benefit.

Departure from Current Public Pension Policy. () Initiating the practice of providing service credit for unused leave accumulation at retirement would establish a new public pension policy in the Commonwealth.

COMMISSION RECOMMENDATION

The Commission voted to attach the actuarial note to the bill, recommending that the General Assembly and the Governor consider the policy issues identified above.

ATTACHMENTS

Actuarial note prepared by William A. Reimert and Katherine A. Warren of Milliman USA.

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