EMPLOYER EDITION January 2008

FACTS At-a-Glance

Ohio Public Employees Retirement System • 277 East Town Street • Columbus, Ohio 43215

Questions or comments?
Contact Employer Reporting at 888-400-0965.

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Specific questions about the Mitigating Contribution Rate for ARPs

The Mitigating Contribution Rate for ARPs

Target audience
This document was prepared for university and college employers who offer alternative retirement plan (ARP) options for their employees. Any university or college employee who works with retirement benefits, especially those who communicate information to employees about retirement options, should read this information.

Overview
By law, a portion of the employer retirement contribution for employees who have selected an alternative retirement plan (ARP) goes to OPERS to help offset the negative financial impact on OPERS. The negative impact results from the costs of administering a retirement system open to all public employees—while still providing retirement plan choices for those same employees. The portion of the employer contribution that goes to defray those costs that OPERS must bear is called a *mitigating rate.*

Under current law, OPERS may collect up to 6% of the employer contribution made on behalf of ARP participants. Effective January 2008, the mitigating rate will be 0.77% of the employer contribution.

Action suggested
Because employers are asked to explain the mitigating rate to their employees, this *Facts At-a-Glance* was prepared to help employers fully understand the complexities of the mitigating rate including:
- Why it is necessary,
- The historical perspective,
- How the mitigating rate is determined, and
- Variables involved.

Please review this document so that you can explain the mitigating contribution and the current rate to your employees who have chosen an ARP.

Additional information available
Previously, an *Employer Notice* was sent to you explaining the 0.77% mitigating rate that will be effective January 1, 2008.

That *Employer Notice* had a draft letter attached that you may want to use to explain the mitigating rate to your employees. Both the letter and the *Employer Notice* have been posted to the OPERS Web site at www.opers.org. In addition, the Employer Call Center is available to help answer your questions.

Employees should contact the Member Services Center with questions at 1-800-222-7377, or they can review the information with their financial advisor or their ARP plan sponsor.

OPERS
1-888-400-0965
www.opers.org

Specific questions about the mitigating contribution rate for ARPs

The question posed was…	The OPERS response is…
What's the background on the mitigating rate?	Effective March 31, 1997, legislation was enacted permitting certain academic and administrative employees of higher education institutions to select an alternative retirement program (ARP) offered by a private vendor in lieu of participating in the appropriate state retirement system. Certain employees (those with less than five years of service and newly hired employees) were permitted to opt out of the state retirement system. To mitigate the negative financial impact of the loss of this population, the law provided for state retirement systems to collect a portion of the employer contribution for those employees who elected to participate in an ARP.
If an employee chooses an ARP, why does OPERS get a part of the employer contribution?	Ohio is a non-Social Security state, meaning that public employees, by law, pay into a state retirement system (such as OPERS) instead of Social Security. If a public employee chooses an ARP instead of OPERS, there is the potential of a negative effect on the state retirement system. Therefore, the Ohio General Assembly mandated that the potential negative impact be mitigated by the collection of a portion of the overall employer contribution, called the mitigating rate. The mitigating rate does not increase the total amount of the employer contribution; it funnels a portion to OPERS.
What is the process for determining the mitigating rate?	Assessing a mitigating rate is entered into only after careful study. The OPERS Board of Trustees works with an independent actuary and the OPERS director of finance each year to determine what, if any, negative financial impact is evolving. In addition, every three years the law requires the Ohio Retirement Study Council to use an independent actuary to review, make projections based on actual information and recommend necessary adjustments in the mitigating rate. These financial professionals work to monitor the level of the financial impact on the state retirement systems that results from offering public employees retirement options such as ARPs. Only after these independent consultants have determined a negative financial impact exists and make recommendations to the OPERS Board of Trustees, does the OPERS Board of Trustees act upon this information and determine what the mitigating rate should be. Then, OPERS notifies its employers with ARP participants of the rate and the implementation date. Each employer then notifies the participants of the implementation date. The most recent review was completed in November 2007.

Specific questions about the mitigating contribution rate for ARPs

The question posed was…	The OPERS response is…
Can the mitigating rate change?	Yes. The mitigating rate can be adjusted up or down. In 1999, OPERS ceased collection of the mitigating rate because the System reached full funding.
What is the negative financial impact?	Funding for state retirement systems is based on average expected employee and employer contributions; retirement contributions are based on a percent of employee salary. The ARP program allows certain employees the option of opting-out of membership. Therefore, a retirement system can be negatively impacted if a portion of the population base is excluded. A portion of every employer contribution is allocated to fund what is referred to as the unfunded liability (see full explanation of this term in the next question). If the pool of new employee-members is diminished, the employer contribution available to fund the unfunded liability is reduced, and the retirement system is negatively impacted.
What causes the unfunded liability?	Unfunded liability is created when a benefit is provided and the appropriate employer and employee contributions (and corresponding investment return) needed to fund the cost of the benefit are not realized. Until a pension system is fully funded, at 100%, there is an unfunded liability. Unfunded liability is also impacted by the amount the retirement system earns on its investments. Investment returns are necessary because only a small portion of the funds you plan to have for retirement come from the actual employee and employer contributions. The more significant component of the retirement savings comes from the investment earnings generated from the long-term investment of the contributions. To the extent retirement systems earn less than anticipated, the unfunded liability grows. Conversely, when retirement systems are able to earn more than anticipated, the unfunded liability is reduced.
Is there a limit on the mitigating rate?	Yes. The law currently authorizes the state retirement systems to collect up to 6% of the employer contribution made on behalf of ARP participants until such time the unfunded pension liability is fully paid. This includes pension benefits only; it does not include the unfunded liability for health care and benefit improvements enacted after the current legislation.

Specific questions about the mitigating contribution rate for ARPs

The question posed was…	The OPERS response is…
What is the history of mitigating rates?	In 1997, H.B. 586 was enacted and OPERS began collecting a mitigating rate of 6%. Beginning January 1, 1999, OPERS reached full funding, which meant there was no unfunded liability. Consequently, OPERS ceased charging a mitigating rate to the ARP participants. The market downturns in 2002-2004 eroded OPERS' funded status—meaning OPERS could have begun charging ARP participants a mitigating rate. However, as mentioned before, these rates are only implemented after careful study and thoughtful recommendation. In addition to the erosion of funded status, the ARP program and other retirement options were expanded in 2005. After careful review of the recommendations made after monitoring the actual negative impact on the funded status of the System, the OPERS Board of Trustees determined to implement a modest mitigating rate in 2007—a rate that will be increased slightly in 2008. Recognizing the potential impact on ARP participants, OPERS chose to implement the lowest mitigating contribution rate possible.
What are the other Ohio statewide retirement systems doing?	Each of the state retirement systems whose populations are eligible to participate in the ARP (OPERS, SERS and STRS) are authorized to collect a mitigating rate to offset the negative financial impact. In 2005, SERS resumed collecting 6% of the employer contribution made on behalf of the ARP participants. Because STRS never reached full funding, that System has continually collected the mitigating contribution rate, which is currently 3.5%.
Is the mitigating rate tied to the increased employer and member contribution rates?	No. The recent stepped increases in employer and member contribution rates were instituted to help reduce unfunded liability, or to strengthen the System—which will ultimately help preserve health care coverage for future generations. The mitigating rate collected from ARP participants is the result of a separate study and different actions—although the actions are not tied together, all are designed to strengthen the System so that pension benefits are preserved.

This fact sheet reviews some of the most common questions and concerns employers have discussed with OPERS about ARPs. Additional assistance is always available by contacting Employer Outreach.