

Senate Bill 117

(With Amendment #1)

Actuarial Cost Study prepared for
Joint Committee on Public Retirement and Social Security Programs
of the Arkansas 94th General Assembly

Provisions of the Bill

Senate Bill 117 affects the Arkansas Teacher Retirement System (ATRS). This bill amends the language of subdivision ACA §24-7-502(a) which defines the separation period before a retired member can be rehired. The bill with Amendment #1 would reduce this separation period from six months to four months.

Fiscal Impact

Senate Bill 117 would allow retired members to be rehired after four months instead of six. In the setting of a normal school year, a person could retire on July 1 and return to work on November 1. This can affect plan costs in two ways. It could make members not feel as risky to retire and retirement rates could go up. It might also encourage people to retire and try to come back to work instead of using the T-DROP program. These possible behavior changes are not as likely with the amended bill's four months (the original was three.) These changes could increase the cost of the plan. There is not good information available to know how much behavior could change so we can't calculate the extent of the increase. Because both situations have a payment of employer contributions without additional accrual, we do not believe the increased cost would significantly impact the total cost of the system.

Other Information

Senate Bill 117 makes a change that introduces a qualification risk to the plan. A separation period shorter than the current six months could open the door to unwritten prearranged agreements that would violate federal separation from service definition. Review the second page for more details. It is our opinion that the four months in Amendment #1 (instead of the original bill's three months) should be long enough to discourage prearrangement.

Related Legislation

Senate Bill 117 would make changes similar to those contained in House Bill 1256. It would be appropriate for the committee to consider the two bills together.

Sincerely,



Jody Carreiro, ASA, MAAA, EA, FCA
Actuary

Separation from Service

Although the phrase "separation from service" is very significant to be a qualified plan under IRS rules, it is not defined in the code or regulations. The courts, using Congressional Committee Reports for guidance, have interpreted separation from service to mean the employee's severing his or her connection with the employer. We can also get a good idea looking at other definitions and various court cases.

Definitely determinable benefits. This is part of what the regulation for 401(a)(1) states: "In order for a pension plan to be a qualified plan under section 401(a), the plan must be established and maintained by an employer primarily to provide systematically for the payment of definitely determinable benefits to its employees over a period of years, usually for life, after retirement or attainment of normal retirement age."

Retirement. The term retirement is used often, usually in the format of "separation from service due to retirement" or "upon retirement". So it is clear that a retirement includes a separation from service.

Revenue rulings and court cases give us several examples of what is not a separation from service.

1. Becoming a partner in a business and no longer a regular employee.
2. A merger or reorganization of businesses when everyone basically continues in the same position (sometimes referred to as a "same seat" rule)
3. Leaving employment and continuing to perform the same services as a contract employee. (There are factors that will allow completely independent contracting).
4. A prearrangement or understanding that you can go back to your job after a period of time. This does not have to be written.

This is why the definition of separation from service often includes a complete severance of all connection with the employer.

In most cases, the statewide Arkansas plans require a six-month waiting period before a retiree can be rehired. The primary concern is prearranged (unwritten) deals to bring someone back or hire them back as they are leaving. It becomes very difficult to make or honor any agreements that far out.