



Pension & Health Benefits Committee

California Public Employees' Retirement System

Agenda Item 5

October 20, 2015

ITEM NAME: Retirement Options Simplification

PROGRAM: Pension

ITEM TYPE: Action

RECOMMEDATION

Staff recommend the Pension & Health Benefits Committee (PHBC) approve condensing the number of retirement payment options from 13 to 5. While the overall options would be reduced, the remaining options available to members would include a combination of existing and modified choices. Approval of this item will allow staff to pursue the necessary regulatory and legislative changes needed to implement the proposed retirement options.

EXECUTIVE SUMMARY

This item is a follow up to the information and recommendations provided to the PHBC in February 2015. This item describes the additional analysis the California Public Employees' Retirement System (CalPERS) staff conducted on the statutory retirement options.

STRATEGIC PLAN

The review of retirement options supports CalPERS Strategic Plan Goal B, to cultivate a high-performing, risk-intelligent, and innovative organization, as well as, CalPERS' Pension Belief that a retirement system must meet the needs of members and employers to be successful.

BACKGROUND

At the February 18, 2015, PHBC meeting, a recommendation was provided to the Board of Administration to eliminate and combine a group of retirement payment options. The recommendation was viewed favorably by the Committee and there was considerable interest in gathering additional data and analysis on other payment options that could lead to further simplifications.

ANALYSIS

Per the Committee's request, staff conducted an additional analysis of retirement payment options. In this latest analysis staff conducted an option comparison using retiree data to determine if a member selected the most beneficial option based on their outcome after retirement.

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Staff analyzed the following data:

- Retirement date
- Option selected
- Member death date
- Beneficiary death date

Additional information on this latest analysis is included in Attachment 1.

Some key findings include:

1. When members chose a reduced retirement allowance in order to provide for a return of contributions if they passed away before those contributions were exhausted (approx. 11 years), 87 percent of the time the member did not benefit from choosing that option.
2. When members chose a reduced retirement allowance speculating their beneficiary would pass away before themselves, 60-70 percent of the time the member did not benefit from choosing that option.
3. The number of options and the varying monetary reductions available to members can be an overwhelming life decision.

Based on these findings, staff concluded the number and complexity of available options are most likely confusing to members and impact their retirement decisions. Staff also believe, condensing and consolidating CalPERS' retirement payment options will lead to better customer service. In addition, the analysis has provided expanded educational opportunities that can be delivered to our members as they consider their retirement options. The information below represents the 13 Retirement Options* and their recommended status:

Pursue simplifying the Retirement Options going forward to the following five options:

Retirement Option	Description
Unmodified	Member Only benefit - Highest Benefit Payable
Option 1	Highest Benefit Payable with Return of Contributions
Option 2W+1	100% Joint Lifetime Benefit with Return of Contributions
Option 3W+1	50% Joint Lifetime Benefit with Return of Contributions
Flexible Beneficiary Option	Joint Lifetime Benefit for Multiple Beneficiaries with choice of dollar amounts

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The following retirement options would be combined with the five simplified retirement options:

Retirement Option	Description
Option 4 - Multiple Lifetime Beneficiaries	Combined into Flexible Beneficiary Option
Option 4 - Specific Percentage to a Beneficiary	Combined into Flexible Beneficiary Option
Option 4 - Specific Dollar Amount to a Beneficiary	Combined into Flexible Beneficiary Option
Option 4 – 2W+1	Combined with statutory Option 2W
Option 4 – 3W+1	Combined with statutory Option 3W

The following retirement options would be eliminated:

Retirement Option	Description
Option 4	Reduced Allowance for a Fixed Period of Time
Option 4	Reduction upon Death of Retiree or Named Beneficiary
Option 2	100% Joint Lifetime Benefit with increase to allowance if beneficiary dies first
Option 3	50% Joint Lifetime Benefit with increase to allowance if beneficiary dies first

* See attachments 2 and 3 for more detailed Retirement Option descriptions.

These recommendations were shared with multiple stakeholder groups during the February timeframe and again this Fall, including labor, employer, school associates and the CalPERS Stakeholder Engagement Group, which includes retiree organizations. These stakeholders responded favorably to our recommendations and are encouraged by the simplification efforts being pursued to meet the needs of our members.

BUDGET AND FISCAL IMPACTS

Revising the retirement payment options would result in one-time administrative costs to CalPERS. The one-time costs include revising publications, educational materials, training materials, and updating the CalPERS website and myCalPERS.

BENEFITS/RISKS

The benefits of eliminating and consolidating retirement options include reducing the complexity of our retirement options for members, improving the customer experience for our retiring members, mitigating member risk in selecting retirement options and simplifying our benefit payment processes, education activities and publications.

Potential risks include legislative and regulatory changes necessary to implement changes, updates to educational materials, temporary increased inquiries from members, and implementing system modifications necessary to accommodate revised options.

ATTACHMENTS

- Attachment 1 – Retirement Options Simplification
- Attachment 2 – Retirement Options Table 1- Current Statutory Options
- Attachment 3 – Retirement Options Table 2- Current Option 4s

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Retirement Options Simplification

Retirement Options Analysis

Staff conducted an Option comparison analysis using retiree data to determine if a member selected the most beneficial Option based on their outcome after retirement. Staff analyzed the following data:

- Retirement date
- Option selected
- Member death date
- Beneficiary death date

Members electing Unmodified Allowance or Option 1, on average, take 10.71 years to deplete their contributions on account. Members electing Option 4- “2W and 1” or Option 4- “3W and 1,” on average, take 12 years to deplete their contributions on account. Staff used these timeframes to determine the beneficial outcomes for Unmodified Allowance, Option 1, Option 4- “2W and 1,” and Option 4- “3W and 1.”

Staff compared the following Options, defining “Beneficial Outcome” for each Option as:

Option	Beneficial Outcome
Unmodified Allowance-	Member lives past 10 years after retirement date
Option 1-	Member lives fewer than 10 years after retirement date
Option 2-	Beneficiary predeceases Member
Option 2W-	Member predeceases Beneficiary
Option 4- 2W and 1 combined-	Both Member and Beneficiary live fewer than 12 years after retirement date
Option 3-	Beneficiary predeceases Member
Option 3W-	Member predeceases Beneficiary
Option 4- 3W and 1 combined-	Both Member and Beneficiary live fewer than 12 years after retirement date

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Retirement Options Simplification, Continued

Unmodified Allowance and Option 1

Members electing Unmodified Allowance assume they will outlive their contributions on account. Members electing Option 1 assume they will not outlive their contributions on account, leaving the remaining contributions to a beneficiary.

The following table compares outcomes for the specified Options:

Benefit Option	Elected Options (1990-2013)	Number of Known Outcomes ¹	Number of Members living beyond 10 years after Retirement Date ²	Number of Members living fewer than 10 years after Retirement Date ³
Unmodified	99,518	62,094	55,458 (89.31%)	6,636 (10.69%)
Option 1	121,741	75,031	65,577 (87.40%)	9,454 (12.6%)

The majority of members electing the Unmodified Allowance and Option 1 live beyond 10.71 years after their retirement date. Based on this data, the Unmodified Allowance was the better Option for this population.

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¹ The known outcome group consists only of cases where at least 10 years have passed since the member's retirement date.

² Members electing Unmodified Allowance or Option 1, on average, take 10.71 years to deplete their contributions on account. Members electing Option 4- "2W and 1" or "3W and 1," on average, take 12 years to deplete their contributions on account.

³ Members electing Unmodified Allowance or Option 1, on average, take 10.71 years to deplete their contributions on account. Members electing Option 4- "2W and 1" or "3W and 1," on average, take 12 years to deplete their contributions on account.

Retirement Options Simplification, Continued

Options 2, 2W, 4- “2W and 1”

Members electing Option 2 assume they will outlive their beneficiary. Option 2 increases a member’s monthly benefit amount to the Unmodified Allowance if their beneficiary predeceases them.

Members electing Option 2W assume their beneficiary will outlive them. Option 2W provides a slightly higher benefit amount than Option 2, but does not increase the benefit amount to the Unmodified Allowance upon their beneficiary’s death.

Members electing Option 4- “2W and 1” assume they and their beneficiary will live fewer than 12 years after their retirement date. Option 4- “2W and 1” provides a secondary beneficiary any remaining contributions on account upon their and their beneficiary’s death.

The following table compares outcomes for the specified Options:

Benefit Option	Elected Options (1990-2013)	Number of Known Outcomes ⁴	Beneficiary Pre-deceases Member	Member Pre-deceases Beneficiary	Both Member and Beneficiary live fewer than 12 years after retirement ⁵
Option 2	76,566	15,183	4,639 (30.55%)	10,544 (69.45%)	1.5%
Option 2W	75,892	13,516	2,485 (18.39%)	11,031 (81.61%)	1.5%
Option 2W+1	46,688	7,525			69 (.92%)

Most members electing Option 2 and Option 2W predecease their beneficiary. For Option 2, Option 2W, and Option 4- “2W and 1,” less than 1 percent of outcomes resulted in both the member and beneficiary living fewer than 12 years after retirement. Based on this data, Option 2W was the better Option for this population.

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⁴ The known outcome group consists only of cases where member, beneficiary, or both are deceased.

⁵ Members electing Unmodified Allowance or Option 1, on average, take 10.71 years to deplete their contributions on account. Members electing Option 4- “2W and 1” or “3W and 1,” on average, take 12 years to deplete their contributions on account.



Retirement Options Simplification, Continued

Options 3, 3W, 4- “3W and 1” Members electing Option 3 assume they will outlive their beneficiary. Option 3 increases a member’s monthly benefit amount to the Unmodified Allowance if their beneficiary predeceases them.

Members electing Option 3W assume their beneficiary will outlive them. Option 3W provides a slightly higher benefit amount than Option 3, but does not increase the benefit amount to the Unmodified Allowance upon their beneficiary’s death.

Members electing Option 4- “3W and 1” assume they and their beneficiary will live fewer than 12 years after their retirement date. Option 4- “3W and 1” provides a secondary beneficiary any remaining contributions on account upon their and their beneficiary’s death.

The following table compares outcomes for the specified Options:

Benefit Option	Elected Options (1990-2013)	Number of Known Outcomes ⁶	Beneficiary Pre-deceases Member	Member Pre-deceases Beneficiary	Both Member and Beneficiary live fewer than 12 years after retirement ⁷
Option 3	31,508	4,253	1,648 (38.75%)	2,605 (61.25%)	1.5%
Option 3W	19,250	2,060	570 (27.67%)	1,490 (72.33%)	1.5%
Option 3W+1	8,724	984			6 (.61%)

Most members electing Option 3 and Option 3W predecease their beneficiary. For Option 3, Option 3W, and Option 4- “3W and 1,” less than 1% of outcomes resulted in both the member and beneficiary living fewer than 12 years after retirement. Based on this data, Option 3W was the better Option for this population.

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⁶ The known outcome group consists only of cases where member, beneficiary, or both are deceased.

⁷ Members electing Unmodified Allowance or Option 1, on average, take 10.71 years to deplete their contributions on account. Members electing Option 4- “2W and 1” or “3W and 1,” on average, take 12 years to deplete their contributions on account.

Retirement Options Simplification, Continued

Pension Reduction Amounts by Option

The Actuarial Office (ACTO) provided calculations for each Option's benefit allowance amount based on a member's age, beneficiary's age, unmodified allowance, and contributions on account. Staff used retiree data to create a profile of the average retiree:

- Average retiree age: 60
- Average Beneficiary age: 55
- Average Unmodified Allowance: \$3,000
- Average Contributions on account: \$100,000

Based on the above profile and actuarial calculations, staff estimate that the average retiree would receive the following benefit under each Option:

Unmodified	1	2	2W	2W+1	3	3W	3W+1
\$3,000	\$2,939	\$2,532	\$2,565	\$2,563	\$2,748	\$2,766	\$2,763
Reduction:	-\$61	-\$468	-\$435	-\$437	-\$252	-\$234	-\$237

Members who do not have a beneficiary or need the maximum benefit amount would likely choose the Unmodified Allowance. Option 1 provides the second highest benefit amount and allows members to provide their beneficiaries any remaining contributions on account. Option 1 costs the member \$61 per month over 10 years to provide a lump sum payment to their beneficiary. If the member lives longer than 10 years, the member will lose approximately \$7,320 over that 10 year period and will not have any contributions remaining on account to leave to his or her beneficiary. The member will lose \$732 per year every year beyond year 10.

Options 2 and 2W provide a lifetime monthly benefit to the member and beneficiary. Option 2 provides the member a smaller monthly benefit amount. If the beneficiary predeceases the member, however, Option 2 increases the member's monthly benefit amount to the Unmodified Allowance, whereas, Option 2W's amount remains the same. Members need to consider the likelihood they will outlive their beneficiaries when choosing between Option 2 and Option 2W. If a member chooses Option 2 and predeceases their beneficiary, then the member paid \$33 per month to receive the pop-up to the Unmodified Allowance that he or she will never receive and provides his or her beneficiary with a smaller continuing monthly benefit than Option 2W.

Retirement Options Simplification, Continued

**Pension
Reduction
Amounts by
Option,
continued**

Options 3 and 3W provide a lifetime monthly benefit to the member and beneficiary. Option 3 provides the member a smaller monthly benefit amount. If the beneficiary predeceases the member, however, Option 3 increases the member's monthly benefit amount to the Unmodified Allowance, whereas, Option 3W's amount remains the same. Members need to consider the likelihood they will outlive their beneficiaries when choosing between Option 3 and Option 3W. If a member chooses Option 3 and predeceases their beneficiary, then the member paid \$18 per month to receive the pop-up to the Unmodified Allowance that he or she will never receive and provides his or her beneficiary with a smaller continuing monthly benefit than Option 3W.

Retirement Options Table 1

Current Statutory Options¹

Option	GC Section	Description
Unmodified Allowance	21350 – 21370	Highest monthly allowance payable to the member; does not provide for a continuing monthly allowance to a beneficiary after the member's death; the only benefit payable is the lump sum death benefit
1	21455	Upon the member's death, pays the unused member contributions to specified beneficiary(ies) in a lump sum; does not provide for a continuing monthly allowance to a beneficiary after the member's death
2	21456	Upon the member's death, pays the same monthly allowance to the member's beneficiary for life and if the member's beneficiary predeceases the member, the member's monthly allowance increases to the Unmodified Allowance
2W	21459	Upon the member's death, pays the same monthly allowance to the member's beneficiary for life and if the member's beneficiary predeceases the member, the member's monthly allowance remains the same
3	21457	Upon the member's death, pays the member's beneficiary half the member's monthly allowance for life and if the member's beneficiary predeceases the member, the member's monthly allowance increases to the Unmodified Allowance
3W	21459	Upon the member's death, pays the member's beneficiary half the member's monthly allowance for life and if the member's beneficiary predeceases the member, the member's monthly allowance remains the same

¹ Option descriptions are from CalPERS, Benefit Services Division *Benefit Estimate Letter (PERS)*.



Retirement Options Table 2

Current Option 4s¹

Option	GC Section	Description
4 – Specific Dollar Amount to a Beneficiary	CCR 585(c)(1)	Upon the member’s death, pays the member’s beneficiary a specified dollar amount of the member’s unmodified allowance
4 – Specific Percentage to a Beneficiary	CCR 585(c)(2)	Upon the member’s death, pays the member’s beneficiary a specified percentage of the member’s unmodified allowance
4 – Option 2W and Option 1 Combined	CCR 585(c)(3)	Upon the member’s death, pays the same monthly allowance to the member’s beneficiary for life; upon the member and the member’s beneficiary’s death, pays any remaining contributions to the member’s secondary beneficiary(ies)
4 – Reduced Allowance for Fixed Period of Time	CCR 585(c)(4)	Pays a specified dollar or percentage of the member’s unmodified allowance to the member for a specified time period and after the specified time period, the member receives an increased allowance based on the actuarial equivalent of their remaining benefit
4 – Multiple Lifetime Beneficiaries	CCR 585(c)(5)	Upon the member’s death, pays a specified dollar or percentage of the member’s unmodified allowance to more than one beneficiary
4 – Option 3W and Option 1 Combined	CCR 585(c)(6)	Upon the member’s death, pays the member’s beneficiary half the member’s monthly allowance for life; upon the member and member’s beneficiary’s death, pays any remaining contributions to the member’s secondary beneficiary(ies)
4 – Reduction upon Death of Retiree or Named Beneficiary	CCR 585(c)(7)	The member specifies a reduction to their unmodified allowance (at least \$1) to provide the highest allowance possible while both the member and the member’s beneficiary are living; upon either the member or member’s beneficiary’s death, the survivor’s continuing allowance is reduced

¹ Option descriptions are from CalPERS, Benefit Services Division *Benefit Estimate Letter (PERS)*.