

# Summary of Considerations included in the Draft DROP Policy

November 1, 2017



# Annuitization Considerations

1. Monthly/Annual Election – 6.14(e)
  - Monthly as the default, 60 days to request annual.
2. Interest Rate – 6.14(e-2)
  - Rates for each quarter are set at the average of the prior 3 months' rates as of the 15<sup>th</sup> of each month based on the U. S. Department of Commerce Daily Treasury Yield Curve Rates. Rates are fixed at the time of annuitization.
  - Life expectancy longer than 30 years will use the 30-year rate.
3. Interest for the period from September 1 to Annuitization Commencement – 6.14(e-2)
  - The annuitization includes interest from September 1, 2017 to the annuitization date, based on the DROP balance as of September 1<sup>st</sup>, adjusted for change in the balance since September 1<sup>st</sup>.
4. Mortality Table – 6.14(e)
  - Life expectancy table was developed by Segal, external actuary, based on their recommended mortality table and is attached to the draft policy.

# Annuitization Considerations

## 5. Payments to Beneficiaries and Alternate Payees – 6.14(g)

- DROP annuity passes to beneficiaries and continues through the original term
- In cases of divorce:
  - If the annuity has already started, the annuity is split based on the QDRO
  - If the annuity has not started, the ex-spouse's annuity (from their portion of the DROP balance) begins at the earlier of 1) start of Member's annuity, or 2) the ex-spouse reaching age 58.

## 6. Revised Annuity Upon Hardship Payment - 6.14(e-3)(2)

- Upon hardship distribution, the amount of the annuity is revised to reflect the distribution using the original interest rate and term.

## 7. De minimis Payment

- The concept has been eliminated for now. A future Board may add the concept at a later date if it is considered to be in the best interest of DPFP.

## 6. Trusts

- The two trusts with DROP accounts that already exist will be annuitized based on the age of the oldest beneficiary.
- Trusts that are named beneficiaries but the Member is still the DROP holder will not be allowed as beneficiaries and the DROP holder will need to provide beneficiary information reflecting a living person.

# Hardship Considerations

- Section 6.14(e-3)(2) reads as follows:

“The Board may by rule allow a DROP participant who has terminated active service and who is eligible for a retirement pension to: ..., 2) in the event of a financial hardship that was not reasonably foreseeable obtain a lump-sum distribution from the participant’s DROP account...”

Although, DROP participant is not a defined term, HB3158 indicates the term is used to refer to a Member or Pensioner.

Therefore, a hardship is only available for the a Retiree Annuitant (Pensioner), not the spouse or a future beneficiary.

- Members entering DROP after HB 3158 passed were aware of the new structure of DROP and the annuitization, therefore, it is recommended that no hardship distributions be allowed for Members entering DROP after June 1, 2017.

# Hardship Considerations

- Circumstances eligible for hardship distribution – 6.14(e-4)

## Current criteria:

- the need to repair damage to the primary residence not covered by insurance as the result of a natural disaster (i.e., flood, etc.);
- the need to make significant changes to the principal residence not covered by insurance because of medical necessity;
- the imminent foreclosure or eviction from a primary residence;
- the need to pay for medical expenses of the DROP account holder, a DROP account holder's spouse or a dependent child or relative as described under IRC sections 152(c) and (d), including non-refundable deductibles, as well as for the cost of prescription drug medication;
- expenses related to an automobile accident involving a DROP account holder not covered by insurance; and
- the need to pay for the funeral expenses of a spouse or a dependent child or relative as described under IRC sections 152(c) and (d)

# Hardship Considerations

- Circumstances eligible for hardship distribution – 6.14(e-4), *continued*

## Proposed expanded criteria in the draft Policy:

- Expanded the need to repair damage to a primary residence not covered by insurance to include *significant events* not only natural disasters. This would include a flood causing *significant* damage or a fire-type event. It is not intended to include deferred maintenance, repair or replacement of normal household items such as furnace, air conditioner, roof, hot water heater, etc.
- Expanded and clarified funeral expenses to include parent, child, grandchild regardless of dependency and to allow necessary associated travel costs.
- The FAFSA-determined Expected Family Contribution amount for Postsecondary education below the graduate level at an eligible institution for a dependent person who is or was a dependent of the Retiree Annuitant.

# Hardship Considerations – 6.14(e-3)

- Hardship administration
  - Staff is not required to seek documentation to validate the DROP holder's certification that "I do not have sufficient assets available or any other financial means to otherwise pay for the expenses detailed in this request"
  - Not allow hardship requests for DROP account holders who have taken prior DROP distributions in excess of \$250,000 prior to June 1, 2017, excluding prior hardship distributions.
- Flexibility – 6.14(e-4)
  - Hardship requests continue to be accepted every 90 days and there is no limit on the number of hardship distribution requests allowed for an Annuitant.

# Revocation Considerations

1. Service purchase: “all or a portion of”
  - All, half or none of the service can be purchased.
2. Calculation of contributions due on a service purchase
  - a. Unpaid contributions
    - To receive credit for additional service time, the Member must pay the difference of the contributions made while in DROP compared to the amount that would have been contributed if the Member had *not* been in DROP, including interest.
  - b. Interest
    - Interest is calculated using the actuarial rate of return assumption used the annual actuarial valuations, compounded annually, from the date the contribution would have been made through the date of service purchase.
  - c. Methodology for determining the cost to purchase a portion of service
    - The cost to purchase half of the time a Member was in DROP is 50% of the cost of purchasing all of the time the Member was in DROP.



# Revocation Considerations

## 3. Contribution payments: sources

- May be made from any source, including any qualified tax deferred account.

## 4. Contribution payments: partial payments & timing

- Full payments of either half or all of the time. Partial payments are not allowed.
- Combined with the recommendation that interest is charged on unpaid contributions at the assumed rate of return, payments can be made at any time prior to the earlier of the Member reentering DROP or retiring.

## 5. Revocation approval

- Board approval of revocation not required.

## 6. Revocation effective date

- Effective upon a completed form being received by DPFP. The Member cannot withdraw their revocation request once it is completed, submitted to and accepted by DPFP.

# Discussion