# TESTIMONY OF SCOTT MILLER

## Engrossed Senate Bill 2046/Proposed Amendment to Close the Defined Benefit Plan

Good Morning/Afternoon, my name is Scott Miller. I am the Executive Director of the North Dakota Public Employees Retirement System, or NDPERS. I appear before you today on behalf of the NDPERS Board in opposition to the proposed amendment to Senate Bill 2046.

SB 2046 was initially proposed by the NDPERS Board, and was the fourth year of the four-year recovery plan the Board initially proposed in 2011, with a single 1% employer contribution and a single 1% employee contribution increase. Note that the Teachers' Fund for Retirement was granted all four years of the same recovery plan back in 2011, and that they have not been back to the Legislative Assembly for additional funding help since that time. That shows that had the Legislative Assembly granted the fourth year of the NDPERS recovery plan back in 2011, we most likely would not be talking about this right now.

The proposed amendment hoghouses 2046, and creates a number of different proposals. I will only discuss the changes that propose to close the Main PERS Defined Benefit (DB) plan and have all new employees go into the Defined Contribution (DC) plan. I anticipate the proponents of this amendment believe it will fix the DB plan. I submit that if such a proposal could actually fix the DB plan, it would have happened years ago, in every state in the country.

I will address the proposed amendment in an outline format.

1. Sections of the amendment on which we suggest clarification or amendment, or for which we have a comment for you to keep in mind.

    a. Section 4 – toward the end of the paragraph, add "participating" to "employees of a political subdivision", so that it reads, "employees of a participating political subdivision". Otherwise this will possibly open the plan up to all political subdivision employees, regardless of whether their employer has signed an agreement to participate.

    b. Section 7. We interpret the new 54-52-02.15 to create a new "political subdivision" retirement plan within the same trust, similar to when the Judges' plan and the Public Safety plans were created. If that is not the intent, that should be clarified.

c. Section 9. Both July 1 and December 1, 2023, are Saturdays. These are the beginning and ending dates for a current DB plan member to make an election into the DC plan. We would suggest moving those dates to weekdays.

d. Section 10. The contribution rate for temporary employees in the amendment includes a contribution for the Retiree Health Insurance Credit. New employees are no longer eligible to participate in the Retiree Health Insurance Credit. We suggest amending this section to remove that contribution.

e. Section 11. This version of the transfer calculation has several issues.

   i. Subsection 54-52.6-03(1) requires us to calculate the present value of a person's accumulated benefit, <u>plus interest since January 1, 2001</u>. I would suggest making that "January 1, 2024".

   ii. Subsection 54-52.6-03(2) requires us to provide a calculation of the member's and employer's contribution, plus interest.

      1. That amount will not be known until the date of transfer, and so members will need to make a decision without this knowledge.

      2. These calculations are very time-intensive because we need to perform research on microfiche to determine contributions for longer-term members.

      3. Historically, about 70% of members have a higher amount under subsection 1.

      4. We suggest removing this calculation, or only making it applicable for non-vested employees since their "accrued benefit" is most likely very small.

   iii. If subsection 2 remains, and is not made applicable only for non-vested employees, we anticipate needing three temp employees for six months to perform the calculations, at a cost of over $86,000.

   iv. If subsection 2 is removed, or is only made applicable for non-vested employees, we anticipate two temp employees for six months would be sufficient, at a cost of just over $57,000. Section 13 seems to assume that we are only providing an advance calculation under subsection 1, so removing or amending subsection 2 as we have suggested would be consistent.

v. Note that every actuarial value transfer from the DB plan to the DC plan will result in an actuarial loss for the DB plan since the DB plan is only 68% funded.

f. Section 14 - $100 million transfer to the state's share of the unfunded liability will provide a windfall for special fund agencies and the sources from which they pay retirement contributions. Right now the general fund only pays for 48% of the employer contribution for state employees. This shifts the responsibility to pay for the plan's unfunded liability from all of these different funding sources 100% to the general fund and legacy fund earnings.

2. Fiscal note –

   a. Temp staffing to complete the required calculations.

   b. Employer contribution increase to compensate for the increase in unfunded liability.

   c. If employer contribution increases are not granted, biennial contributions for us to make benefit payments.

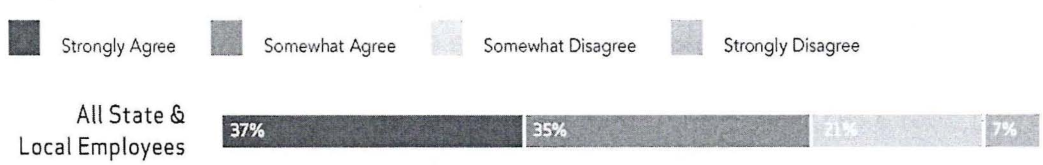
3. Actuarial analysis – one week to complete analysis once Employee Benefits Programs Committee accepts jurisdiction of the amended bill; $20,000.

4. Personnel Considerations

   a. Public employees overwhelmingly prefer a defined benefit plan ("State and Local Employee Views on Their Jobs, Pay and Benefits" by Tyler Bond and Kelly Kenneally, National Institute on Retirement Security, 2019)

Figure 22: **Across professions, state and local employees overwhelmingly agree that a pension benefit is a major reason they chose a public sector job.**

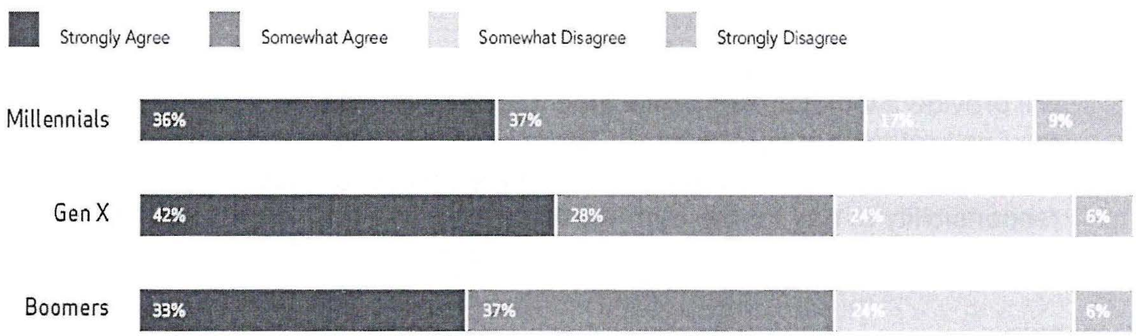
To what extent do you agree or disagree with the following statement: A pension benefit is a major reason I chose a public sector job in the first place.




   b. This is true for millennials, as well

Figure 70: **74% of Millennial state and local employees say a pension benefit is a major reason they chose a public sector job.**

To what extent do you agree or disagree with the following statement: A pension benefit is a major reason why I chose a public sector job.




c. Previous experience with "irrevocable" elections to transfer from the DB Plan to the DC plan aligns with these studies.

   i. The NDPERS retirement plan was originally a cash-balance DC plan, which the Legislative Assembly changed to a DB plan in 1977 because the DC plan was not providing a secure retirement for its employees; DC plan employees were given several opportunities to elect to transition to the DB plan

   ii. The 2013 Legislative Assembly expanded the eligibility for the DC plan to include <u>all</u> new employees

   iii. Only 3% of new employees chose the DC plan

   iv. Buyer's remorse soon set in, and DC plan members lobbied the Legislative Assembly to allow them to transfer back into the DB plan

   v. In 2017, the Legislative Assembly opened a window for DC plan members to move back into the DB plan

   vi. <u>75% of our DC plan members elected to transfer back into the DB plan</u>

   vii. We currently have less than 100 active employees in our DC plan

d. Moving from a DB plan to a DC plan results in a reduction in benefits; compensation increases and other benefit increases will be necessary to recruit and retain quality employees

e. The NDPERS plan is already a hybrid DB/DC plan because of the addition of the Portability Enhancement Provision (PEP) in 1999: short-term employees who also participate in our 457 deferred compensation plan already can take a portion of the employer contributions when they leave employment, which includes guaranteed interest

5. Fiscal Considerations

   a. This bill would render meaningless all of the efforts to stabilize the Main PERS plan over the past ten years, the employee and employer increases, the reductions in benefits, everything

   b. The forced liquidation of trust fund assets to fund the transfers from the DB plan to the DC plan may significantly affect our investment portfolio, and reduce our earnings.

   c. DB closure bills have been proposed in nearly every session staff can remember, and there have been many studies of such proposals as a result.

   d. In 2014, the Legislative Assembly contracted with the actuarial firm Arthur J. Gallagher & Co. to perform an independent analysis of the one-time cost to close the DB plan. Based on the DB plan's situation and the actuarial analysis at the time, Gallagher determined that a one-time contribution of $445 million was necessary if the DB plan was closed for all new employees.

   e. Perhaps the most comparative example of the probable impact of this amendment is from Representative Steiner's 2018 proposal that was considered by the 2017-2019 Employee Benefits Programs Committee ("Bill 382").

      i. That bill would have:

         1. Transferred <u>$108 million per year</u> from the Legacy Fund principal into the NDPERS fund until it was 95% funded

         2. Closed the defined benefit DB plan to new state employees (<u>not</u> political subdivision employees) after December 31, 2019

         3. All new state employees would have gone into the DC plan

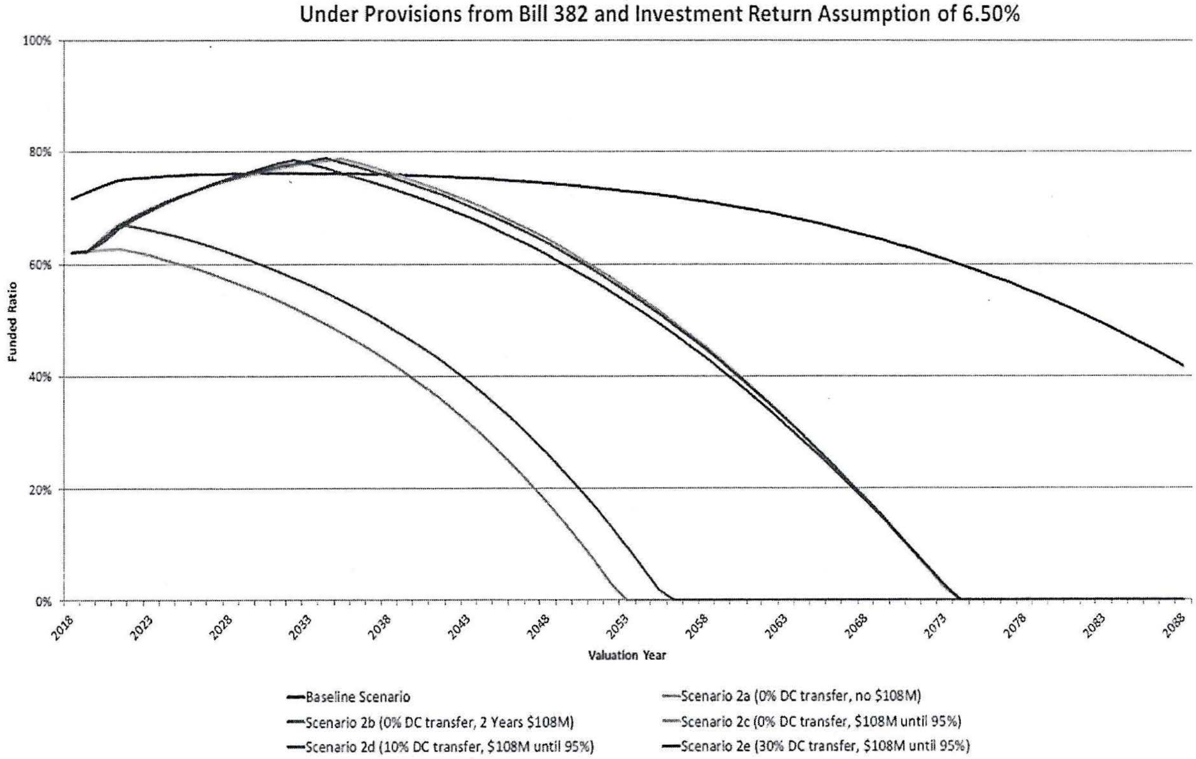
         4. Allowed current state DB plan members to elect to transfer into the DC plan

ii. At that time the Main NDPERS plan was projected to become insolvent by 2106

iii. The result of the actuarial analysis of that proposal was that the Main NDPERS plan would become insolvent much earlier (between 2040 and 2074) as a result of closing the DB plan, as you can see in the below table (yellow highlight) and graph.

| Scenario | Investment Return Assumption/ Discount Rate (Liabilities) | Percent of Current Active Members Transferring to the Defined Contribution Plan | Last Year of $108 Million Contributions (When State Funded Status attains 95%) | Funded Ratio in 2048 | | | Year Assets are Depleted | | | Present Value of Future Total Contributions (In Millions) | Present Value of Benefits and Expenses (In Millions) |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | State | Political Subdivisions | Total Main System | State | Political Subdivisions | Total Main System | | |
| Baseline - July 1, 2018 Valuation | 7.75% | NA | NA | 74.24% | 74.24% | 74.24% | NA | NA | 2106 | $ 4,230 | $ 7,148 |
| Bill 382 - Scenario 1a | 5.50% | 0% | None | 0.00% | 31.17% | 0.00% | 2040 | 2065 | 2048 | 5,108 | 11,266 |
| Bill 382 - Scenario 1b | 5.50% | 0% | 2021 | 0.00% | 31.17% | 5.62% | 2043 | 2065 | 2050 | 5,303 | 11,266 |
| Bill 382 - Scenario 1c | 5.50% | 0% | 2063 | 79.11% | 31.17% | 46.75% | 2082 | 2065 | 2068 | 6,839 | 11,266 |
| Bill 382 - Scenario 1d | 5.50% | 10% | 2054 | 86.58% | 31.17% | 48.15% | 2077 | 2065 | 2068 | 6,645 | 11,091 |
| Bill 382 - Scenario 1e | 5.50% | 30% | 2044 | 94.22% | 31.17% | 47.90% | 2072 | 2065 | 2067 | 6,272 | 10,741 |
| Bill 382 - Scenario 2a | 6.50% | 0% | None | 0.00% | 50.91% | 17.36% | 2043 | 2076 | 2053 | 3,888 | 8,408 |
| Bill 382 - Scenario 2b | 6.50% | 0% | 2021 | 0.00% | 50.91% | 26.12% | 2046 | 2076 | 2056 | 4,078 | 8,408 |
| Bill 382 - Scenario 2c | 6.50% | 0% | 2035 | 91.18% | 50.91% | 64.32% | 2069 | 2076 | 2074 | 4,910 | 8,408 |
| Bill 382 - Scenario 2d | 6.50% | 10% | 2034 | 91.04% | 50.91% | 63.58% | 2069 | 2076 | 2074 | 4,798 | 8,289 |
| Bill 382 - Scenario 2e | 6.50% | 30% | 2032 | 89.22% | 50.91% | 61.55% | 2068 | 2076 | 2074 | 4,565 | 8,049 |

Main System
Projected Funded Ratio (Actuarial Value of Assets)
Based on July 1, 2018 Actuarial Valuation
Under Provisions from Bill 382 and Investment Return Assumption of 6.50%



iv. This proposed amendment would most likely cause the Main NDPERS plan to become insolvent even earlier, for three primary reasons:

1. The proposed amendment only deposits about 20% of the money proposed in Bill 382

2. The current assumed rate of return is 7%, instead of the 7.75% in 2018, so the average investment return assumption will be lower than the 6.5% in this graph

3. Right now we are only 68.3% funded, whereas we were 71.6% funded in 2016 – a $150 million difference

v. Because the benefit reductions from the 2019 session have only been in effect for two years, their effect would be minimal

vi. Because this amendment would cause the plan to become insolvent so much earlier, the GASB liability amount that the State will have to report on its financial statements will significantly increase, possibly affecting the State's bond ratings

6. Conclusion

a. There are a number of sections within the proposed amendment that require clarification or amendment

b. The fiscal impact of the proposed amendment results in the need for a fiscal note if it is adopted

c. An actuarial analysis is necessary to understand the full impact of this amendment

d. There are a number of personnel concerns to consider as you deliberate on this bill

i. The past experience with DC plans for state employees that resulted in employee dissatisfaction and many hours of legislative consideration to review and address those concerns, and eventually allow them to return to the DB plan

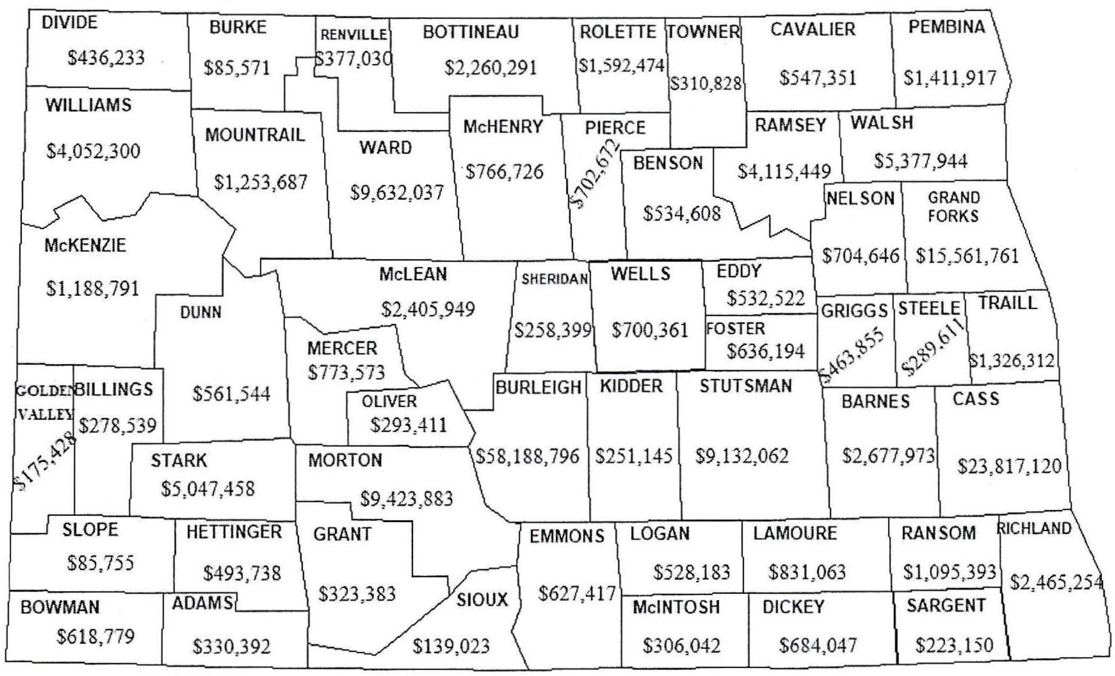
ii. This bill will de-stabilize the Main PERS plan, affecting the retirement security of over 50,000 North Dakotans in every county in the state

e. Finally, and most importantly, this proposed amendment will result in the State's defined benefit plan becoming insolvent within our lifetimes.

This proposed amendment does not "fix" the defined benefit plan; if it were this easy, it would have happened years ago, in every state in the country. What it will do is cause the trust to be completely drained of all funds – state, political subdivision, judge's, and public safety – within the next fifty years. At that point, the Legislative Assembly will need to appropriate hundreds of millions of dollars every biennium for us to make benefit payments, for state and political subdivision, judges, and public safety retirees.

## NDPERS Retirees

Annual Benefits 2019




Out-of-State - $28,090,553

Total - $204,988,624