NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

EMPLOYEE BENEFITS PROGRAMS COMMITTEE

Wednesday, November 17, 1999
Harvest Room, State Capitol
Bismarck, North Dakota

Representative Jim Poolman, Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives Jim Poolman, Glen Froseth, Bette Grande, Serenus Hoffner, Joe Kroeber; Senators Ralph Kilzer, Carolyn Nelson, Herb Urlacher

Member absent: Senator Karen K. Krebsbach

Others present: See Appendix A

It was moved by Senator Nelson, seconded by Senator Kilzer, and carried that the minutes of the June 24, 1999, committee meeting be approved as distributed.

TEACHERS' FUND FOR RETIREMENT

At the request of Chairman Poolman, Mr. Chris Conradi, Actuary, Watson Wyatt Worldwide, Dallas, Texas, presented the July 1, 1999, actuarial valuation of the Teachers' Fund for Retirement. A copy of the actuarial valuation is on file in the Legislative Council office and a copy of the overheads used by Mr. Conradi in his presentation is attached as Appendix B. He said there were 10,046 active members and 4,568 retired members in the Teachers' Fund for Retirement as of July 1, 1999. He said there were 9,896 active members on June 30, 1998. He noted there are usually fewer active members in years after a legislative session because benefit enhancements enacted by the Legislative Assembly usually result in an increased number of retirements in those years. He said the active payroll was $314.6 million on July 1, 1999, and the average salary was $31,318. He said the average annual benefit on July 1, 1999, was $9,995. The market value of assets in the Teachers' Fund for Retirement, on July 1, 1999, he said, was $1,262,600,000 with an actuarial value of $1,053,100,000.

In response to a question from Representative Poolman, Mr. Conradi said the unfunded liability of the Teachers' Fund for Retirement should not be viewed as an accounting liability but almost as a fictitious liability. He said the unfunded actuarial accrued liability is $135.3 million, but is at an acceptable level.

In response to a question from Representative Grande, Mr. Conradi said contributions are essentially matching benefit payments and the system could easily withstand a decrease of four or five percent in the number of active members.

Chairman Poolman recognized Senator Nelson. She reminded the committee that the assumptions used by Watson Wyatt Worldwide in its actuarial valuation are made by the Board of Trustees of the Teachers' Fund for Retirement with the advice of its actuaries.

Mr. Conradi said the Teachers' Fund for Retirement is 88.6 percent funded and the unfunded actuarial accrued liability as a percentage of payroll is 43 percent. He said the required contribution rate for the plan year is 6.09 percent and the statutory contribution rate is 7.75 percent. Thus, he said, the current margin available is 1.66 percent of payroll or 7.75 - 6.09 = 1.66.

PUBLIC EMPLOYEES RETIREMENT SYSTEM

At the request of Chairman Poolman, Mr. Roderick B. Crane, Vice President, The Segal Company, Denver, Colorado, presented the July 1, 1999, actuarial valuations of the Public Employees Retirement System main system, judges' retirement fund, National Guard retirement fund, Highway Patrolmen's retirement fund, and the retiree health benefits fund. The actuarial valuation reports for the North Dakota Public Employees Retirement System, North Dakota Highway Patrolmen's retirement system, and the North Dakota Public Employees Retirement System retiree health insurance credit fund are on file in the Legislative Council office and a copy of the overheads used by Mr. Crane in his presentation is attached as Appendix C. He said all systems have positive contribution margins and benefit improvements are reflected in all liabilities. He said return on the actuarial value of assets exceeded the return on the market value of assets, which means the smoothing mechanism is at work. He noted that the funded ratio is near or above 100 percent for all plans except the retiree health insurance credit fund, but that fund improved from 29.7 percent to 33.7 percent. Thus, he said, investments in the retiree health insurance credit fund are growing more rapidly than liabilities.

Mr. Crane reviewed benefit improvements made by the 1999 Legislative Assembly to the main and National Guard retirement systems. He said the benefit multiplier was increased from 1.77 percent to 1.89 percent; a portability enhancement provision was enacted; vesting and early retirement and preretirement death eligibility service was decreased from five years to three years; an ad hoc increase of eight percent was provided to retirees, disabled members, and beneficiaries; and finally, the normal retirement service requirement was decreased from five years to three years for the National Guard retirement system. Concerning the judges' retirement plan, he said, the 1999 Legislative Assembly increased the disability benefit from 25 percent of final average salary to 70 percent of final average salary less Social Security and workers' compensation benefits. He said the Legislative Assembly increased the death benefit to the greater of the lump sum of employee contributions or 100 percent of the unreduced accrued benefit and provided an ad hoc postretirement increase of two percent on January 1, 2000, and two percent on January 1, 2001.

Concerning the July 1, 1999, actuarial valuation of the Public Employees Retirement System and the Highway Patrolmen's retirement system, Mr. Crane said the combined assets, at market value, totaled $1.14 billion. He said these assets had an actuarial value of $949 million or 83 percent of the market value. The rate of return on actuarial assets over the past year, he said, was 14.72 percent or 6.72 percent higher than the eight percent actuarially assumed rate of return. He said the 10-year average rate of return was 11.09 percent. He said the employer cost rate for 1999 is 3.34 percent of payroll and the statutory contribution rate is 4.12 percent of payroll. Thus, he said, the available margin on July 1, 1999, was .78 percent of payroll or 4.12 percent - 3.34 percent = .78 percent. He said the employer cost rate for the judges' retirement system is 7.36 percent of payroll and the statutory contribution rate is 14.52 percent of payroll. Thus, he said, the margin in the judges' retirement fund is 7.16 percent or 14.52 percent - 7.36 percent = 7.16 percent of payroll. He said the employer cost rate for the National Guard retirement fund is 3.84 percent and the contribution rate set by the Public Employees Retirement System Board is 8.33 percent. Thus, he said, the margin available in the National Guard retirement fund is 4.49 percent or 8.33 percent - 3.84 percent = 4.49 percent.

In response to a question from Representative Poolman, Mr. Crane said if there is an available margin in a retirement fund, the Legislative Assembly has the option of enhancing benefits or reducing employer contributions to the retirement system.

Concerning the margin available in the judges' retirement system, Mr. Crane said historically the Legislative Assembly has maintained a large margin in this plan. The reason for this, he said, is that it is a small plan with a small number of participants and if there were several unexpected retirements it would have a major impact on the fund.

In response to a question from Representative Poolman, Mr. Crane said the employer contributions for the various retirement funds have not been reduced or increased since they were established. However, he noted, one percent of the employer contribution has been diverted to fund the retiree health benefits fund.

Chairman Poolman recognized Mr. Sparb Collins, Executive Director, Public Employees Retirement System. Mr. Collins said when the Public Employees Retirement System was established in 1977, the multiplier was 1.04 percent and there was an unfunded liability. Since that time, he said, the employer contribution has not changed, but investment gains have been used to reduce the unfunded liability and to increase the multiplier from 1.04 percent to 1.89 percent. Also, he said, investment gains have been used to provide other enhancements to the retirement system such as the rule of 85 and ad hoc adjustments for retirees.

In summary, Mr. Crane said there is no unfunded actuarial accrued liability in the main, judges', or National Guard retirement systems.

Concerning the retiree health insurance credit fund, Mr. Crane said the fund had assets, at market value, as of July 1, 1999, of $23.4 million with an actuarial value of $19.4 million or 83 percent of market value. The market value rate of return during the past year was 12.18 percent while the actuarial value rate of return was 15.1 percent or 7.15 percent in excess of the 8 percent investment assumptions. He said the employer cost rate for 1999 was .99 percent while the statutory contribution rate is 1.00 percent, leaving a margin of .01 percent in the retiree health benefits fund.

Concerning the Highway Patrolmen's retirement system, Mr. Crane said the employer cost rate for 1999 is 11.87 percent and the statutory contribution rate is 16.70 percent of payroll. Thus, he said, the available margin is 4.83 percent or 16.70 - 11.87 = 4.83.

VENDOR STUDY

Chairman Poolman called on Mr. Collins, who distributed a summary of investment options for the deferred compensation plan and a brochure describing the portability enhancement provision enacted by the 1999 Legislative Assembly. These items are on file in the Legislative Council office. Mr. Collins also distributed a memorandum listing the number of participants by provider in the deferred compensation program and a member survey of benefits provided by the North Dakota Public Employees Retirement System, copies of which are attached as Appendices D and E, respectively.

In response to a question from Representative Poolman, Mr. Collins said to be an approved provider, a deferred compensation provider must have 50 participants and sign a participation agreement with the Public Employees Retirement System Board. He said only two of the current providers, the Public

Employees Retirement System companion plan managed by VALIC and Waddell and Reed, provide mutual funds while the other providers provide annuity products.

Chairman Poolman called on Ms. Sandy Fotiades, Vice President, Fidelity Investments Public Sector Services Company, Boston, Massachusetts, who said Fidelity Investments had just completed a conversion for the state of Delaware's 457 deferred compensation plan from five providers to a single provider. Ms. Fotiades said many plan sponsors are moving to a semi-bundled approach. She said it has been Fidelity's experience that if a participant can look to one provider for education, it improves education, asset allocation, and returns for participants. From the state's perspective, she said, if all the deferred compensation assets are bundled together and made available to one provider, it will lead to reduced fees for participants with more of the participants' dollars being invested in their retirement accounts which leads to a greater amount of money being available to participants at retirement.

Chairman Poolman called on Mr. Wayne Muehler, Investment Centers of America, who said the current situation with 13 vendors is working very well and provides state employees with a choice of deferred compensation vendors. Mr. Muehler said if the current situation is not broken, the Legislative Assembly should not endeavor to fix it.

Chairman Poolman called on Mr. Bill Blanchard, VALIC, Minneapolis, Minnesota, who noted that Minnesota went from 130 deferred compensation providers to four. However, Mr. Blanchard said the state did not consult the end user, the participants. He said the committee should get input from the participants before it limits their choice of vendors.

Chairman Poolman called on Mr. Peter J. Otte, Division Manager, Waddell and Reed Financial Services. A copy Mr. Otte's written comments is attached as Appendix F. In response to Ms. Fotiades' comments, Mr. Otte agreed that ease of administration is a concern of the state, but that choice, service, and education are more important.

In response to Mr. Otte's comments, Representative Poolman said the committee is not interested in limiting competition but is interested in best serving the interests of the employees of the state of North Dakota.

Chairman Poolman called on Mr. Roger Koski, American Express Advisors, who said today's consumers are looking for choice in the provision of investment services.

Concerning implementation of the defined contribution retirement plan, Mr. Collins said the legislation authorizing the defined contribution retirement plan contained a provision authorizing the Public Employees Retirement System Board to provide a mechanism to allow a portion of the contribution to be used to provide disability insurance. However, he said, if employees are allowed to make an election for a present benefit with pretax moneys, the contribution becomes taxable. Another portion of the bill, he said, provided that all funds must be put aside on a pretax basis. To resolve this conflict, he said, the Public Employees Retirement System Board has determined not to offer a disability component in the defined contribution plan. However, he said, the board has included a provision in the plan to allow members to access their accumulated account balance for a disability benefit in the amount of the balance should they become disabled. Finally, he noted, individuals may purchase disability insurance on their own using other funds.

At the request of Chairman Poolman, Ms. Fotiades reviewed the implementation of the defined contribution retirement plan. A copy of her presentation is on file in the Legislative Council office. She reviewed the public sector experience of Fidelity Investments Tax-Exempt Services Company, its approach to implementing the defined contribution retirement plan, the investment education provided by Fidelity, participant and plan sponsor services provided by Fidelity, and the investment options available under the defined contribution retirement plan. She also reviewed the enrollment strategy consisting of participant election and the first contributions to the defined contribution retirement plan and the strategy that Fidelity and the state plan to use for new hires.

In response to a question from Representative Froseth, Mr. Collins said the participants in a defined contribution retirement plan will be charged an $8 administrative fee as well as a fee of six basis points. He said participants must be employed on December 31, 1999, and must be employed through the date of the transfer of funds to their defined contribution account. He said if an employee terminates prior to completion of the transfer, that employee must remain in the defined benefit plan. He said the election is a one-time irrevocable decision and that new employees joining the state after December 31, 1999, have a six-month window in which to decide which plan to join.

In response to a question from Representative Poolman, Mr. Collins said he would update the committee on the number of employees who transfer to the defined contribution retirement plan as well as provide a statistical profile of the group transferring and the impact on the defined benefit retirement plan.

In response to a question from Representative Poolman, Ms. Fotiades said Michigan, Vermont, Montana, and Arizona have recently established defined contribution retirement plans for certain groups of employees and 23 states are studying the issue this year. She said 43 percent of the eligible employees transferred to the new defined contribution plan in Vermont.

Chairman Poolman called on Mr. Cy Puetz, AXA Advisors/Equitable, who said he is a proponent of multiple providers and that Equitable has been involved with the deferred compensation program since its inception. He said Equitable holds approximately $72 million for its clients, not counting accounts that have been annuitized and are paying benefits to retirees.

Chairman Poolman called on Mr. Hal Mayden, Great West Life, Denver, Colorado, who said participants in the deferred compensation program have been served very well by the providers currently in the program and that participants are pleased. Mr. Mayden said changing to one vendor may have a very serious and dramatic impact on participants' perception of the deferred compensation program. He distributed a survey of state deferred compensation plans prepared by Benefits Communications Corporation, a copy of which is on file in the Legislative Council office. He said most states have gone to a bundled plan design with one administrator. However, he said, there are still 10 states with multivendor programs.

Chairman Poolman called on Mr. Greg Gunderson, Investment Centers of America, who said his firm believes education is the key to providing good service and increasing participation in the deferred compensation program and that limiting the number of providers would lessen the opportunity to provide education and ultimately participation in the deferred compensation program.

Chairman Poolman called on Mr. Lyle Lauritsen, AETNA, Fargo, who said he has had trouble contacting state employees and some supervisors are reluctant to give his company access to their employees. He said supervisors should inform their employees of the availability of the deferred compensation program and allow providers access to their employees to inform them and educate them about the availability of this benefit.

Chairman Poolman called on Ms. Theresa Hall-Biesecker, AXA Advisors/Equitable, who said she has had trouble accessing state employees and many supervisors and departments restrict their employees' access to deferred compensation providers. Ms. Hall-Biesecker said AXA Advisors/Equitable provides an indepth educational process when they get the opportunity to meet with potential clients to inform them of the benefits of participating in a deferred compensation program as well as its place in their total financial picture.

In response to a question from Representative Froseth, Mr. Collins said the Public Employees Retirement System Board does not know what impact the creation of the defined contribution retirement plan will have on the defined benefit program. However, he said, due to the small number of employees eligible to participate in the new defined contribution retirement program, the impact will be small and may even be beneficial depending upon the number and characteristics of the employees who transfer.

At the request of Chairman Poolman, committee counsel reviewed the procedure established by the committee for submitting bills to the committee. He said only legislators and state agencies with the bill introduction privilege may submit bills to the committee, that the proposals must be in bill draft form, and that the proposals must be submitted prior to April 1, 2000. He said the Legislative Council staff will provide bill drafting services for legislators and state agencies should contact the assistant attorney general assigned to that agency for bill drafting advice. Traditionally, he said, bills submitted to the committee have had at least three hearings--the meeting at which the bill is submitted, the meeting at which affected individuals are allowed to testify concerning the bill, and the meeting at which the actuarial report on the bill is received. He said he will send out a reminder notice to legislators and state agencies with the bill introduction privilege in February reminding them of the April 1, 2000, deadline.

No further business appearing, Chairman Poolman adjourned the meeting at 3:30 p.m.

Jeffrey N. Nelson
Committee Counsel

ATTACH:6