EMPLOYEE BENEFITS PROGRAMS COMMITTEE

The Employee Benefits Programs Committee has statutory jurisdiction over legislative measures that affect retirement, health insurance, and retiree health insurance programs of public employees. Under North Dakota Century Code (NDCC) Section 54-35-02.4, the committee is required to consider and report on legislative measures and proposals over which it takes jurisdiction and which affect, actuarially or otherwise, retirement programs and health and retiree health plans of public employees. Section 54-35-02.4 also requires the committee to take jurisdiction over any measure or proposal that authorizes an automatic increase or other change in benefits beyond the ensuing biennium which would not require legislative approval and to include in the report of the committee a statement that the proposal would allow future changes without legislative involvement. The committee is allowed to solicit draft measures from interested persons during the interim and is required to make a thorough review of any measure or proposal it takes under its jurisdiction, including an actuarial review. A copy of the committee's report must accompany any measure or amendment affecting a public employee's retirement program, health plan, or retiree health plan which is introduced during a legislative session. The statute provides that any legislation enacted in contravention of these requirements is invalid and benefits provided under that legislation must be reduced to the level in effect before enactment. In addition, Section 54-52.1-08.2 requires the committee to approve terminology adopted by the Public Employees Retirement System (PERS) Board to comply with federal requirements and Section 18-11-15 requires the committee to receive notice from a firefighters relief association concerning service benefits paid under a special schedule.

Pursuant to NDCC Section 54-06-31, the Legislative Council assigned the committee the responsibility to receive periodic reports from the Human Resource Management Services Division of the Office of Management and Budget on the implementation, progress, and bonuses provided under state agency recruitment and retention bonus programs. The Legislative Council also assigned to the committee a study directed by Section 28 of House Bill No. 1015 (2005) of issues relating to state employee compensation.

Committee members were Representatives Matthew M. Klein (Chairman), Al Carlson, Joe Kroeber, Ken Svedjan, and Francis J. Wald and Senators Ray Holmberg, Ralph L. Kilzer, Karen K. Krebsbach, and Carolyn Nelson.

The committee submitted this report to the Legislative Council at the biennial meeting of the Council in November 2006. The Council accepted the report for submission to the 60th Legislative Assembly.

CONSIDERATION OF RETIREMENT AND HEALTH PLAN PROPOSALS

The committee established April 1, 2006, as the deadline for submission of retirement, health insurance, and retiree health proposals and July 1, 2006, as the deadline for submission of health insurance mandate proposals. The deadlines provide the committee and the consulting actuary of each affected retirement, health, or retiree health program sufficient time to discuss and evaluate the proposals. The committee allowed only legislators and those agencies entitled to the bill introduction privilege to submit proposals for consideration.

The committee reviewed each submitted proposal and solicited testimony from proponents, retirement and health program administrators, interest groups, and other interested persons.

Under NDCC Section 54-35-02.4, each retirement, insurance, or retiree insurance program is required to pay, from its retirement, insurance, or retiree health benefits fund, as appropriate, and without the need for a prior appropriation, the cost of any actuarial report required by the committee which relates to that program.

The committee referred the proposals submitted to it to the affected retirement or insurance program and requested the program authorize the preparation of actuarial reports. The Public Employees Retirement System used the actuarial services of The Segal Company in evaluating proposals that affected retirement programs and the actuarial services of Gallagher Benefit Services, Inc., in evaluating proposals that affected the public employees health insurance program. The Teachers' Fund for Retirement (TFFR) Board of Trustees used the actuarial services of Gabriel, Roeder, Smith and Company in evaluating proposals that affected the Teachers' Fund for Retirement.

The committee obtained written actuarial information on each proposal. In evaluating each proposal, the committee considered the proposal's actuarial cost impact; testimony by retirement and health insurance program administrators, interest groups, and affected individuals; the impact on the state general fund or special funds and on the affected retirement program; and other consequences of the proposal or alternatives to it. Based on these factors, each proposal received a favorable recommendation, unfavorable recommendation, or no recommendation.

A copy of the actuarial evaluation and the committee's report on each proposal will be appended to the proposal and delivered to its sponsor. Each sponsor is responsible for introducing the proposal to the 60th Legislative Assembly.

TEACHERS' FUND FOR RETIREMENT

History

Former NDCC Chapter 15-39 established the teachers' insurance and retirement fund. This fund, the rights to which were preserved by Section 15-39.1-03, provides a fixed annuity for full-time teachers whose rights vested in the fund before July 1, 1971. The plan was repealed in 1971 when the Teachers' Fund for Retirement was established with the enactment of Chapter 15-39.1. The plan is managed by the TFFR Board of Trustees.

The Teachers' Fund for Retirement became effective July 1, 1971, and is administered by a board of trustees. A separate state investment board is responsible for the investment of the trust assets, although the TFFR Board of Trustees establishes the asset allocation policy. The Retirement and Investment Office is the administrative agency for the Teachers' Fund for Retirement. The Teachers' Fund for Retirement is a qualified governmental defined benefit retirement plan. For Governmental Accounting Standards Board purposes, it is a cost-sharing, multiple-employer public employee retirement system.

Contribution Rates and Benefits

Every certified teacher of a public school in the state participates in the Teachers' Fund for Retirement. This includes teachers, supervisors, principals, and administrators. Noncertified employees such as teacher's aides, janitors, secretaries, and drivers are not allowed to participate in the Teachers' Fund for Retirement. Eligible employees become members at the date of employment.

An active member contributes 7.75 percent of salary per year. The employer may "pick up" the member's assessments under Internal Revenue Code Section 414(h). The member's total earnings are used for salary purposes, including overtime, and including nontaxable wages under a Section 125 plan, but excluding certain extraordinary compensation, such as fringe benefits or unused sick or vacation leave.

The district or other employer that employs a member contributes 7.75 percent of the member's salary. Employees receive credit for service while members. A member may also purchase credit for certain periods, such as time spent teaching at a public school in another state, by paying the actuarially determined cost of the additional service. Special rules and limits govern the purchase of additional service.

A member is eligible for a normal service retirement benefit at age 65 with credit for three years of service or when the sum of the member's age and years of service is at least 85--the Rule of 85. The monthly retirement benefit is 2.00 percent of final average compensation, defined as the average of the member's highest three-plan year salaries with monthly benefits based on one-twelfth of this amount, times years of service. Benefits are paid as a monthly life annuity, with a guarantee that if the payments made do not exceed the member's assessments plus interest, determined as of the date of retirement, the balance will be paid in a lump sum to the member's beneficiary.

A member may retire early after reaching age 55 with credit for three years of service. In this event, the monthly benefit is 2.00 percent of final average compensation times years of service, multiplied by a factor that reduces the benefit 6 percent for each year from the earlier of age 65 or the age at which current service plus age equals 85.

A member is eligible for disability retirement benefits provided the member has credit for at least one year of service. The monthly disability retirement benefit is the greater of the amount of retirement benefits without consideration of age or the amount of retirement benefits without consideration of age assuming the member had 20 years of service. The disability benefit commences immediately upon the member's retirement. Benefits cease upon recovery or reemployment. Disability benefits are payable as a monthly life annuity with a guarantee that, at the member's death, the sum of the member's assessments plus interest as of the date of retirement that is in excess of the sum of payments already received will be paid in a lump sum to the member's beneficiary. All alternative forms of payment are also permitted in the case of disability retirement. Disability benefits are converted to normal retirement benefits when the member reaches normal retirement age or age 65, whichever is earlier.

A member with at least three years of service who does not withdraw contributions from the fund is eligible for a deferred termination benefit. The deferred termination benefit is a monthly benefit of 2.00 percent of final average compensation times years of service. Final average compensation and service are determined at the time the member leaves active employment. Benefits may commence unreduced at age 65 or when the Rule of 85 is met. Reduced benefits may commence at or after age 55 if the member is not eligible for an unreduced benefit. The form of payment is the same as for normal retirement.

A member leaving covered employment with less than three years of service is eligible to withdraw or receive a refund benefit. Optionally, a vested member (with three or more years of service) may withdraw assessments plus interest in lieu of the deferred benefits otherwise due. A member who withdraws receives a lump sum payment of employee assessments, plus the interest credited at 6 percent on these contributions.

To receive a death benefit, death must have occurred while the person was an active or inactive, nonretired member. Upon the death of a nonvested member, a refund of the member's assessments and interest is paid. Upon the death of a vested member, the beneficiary may elect the refund benefit; payment for 60 months of the normal retirement benefit, based on final average compensation and service determined at the date of death; or a life annuity of the normal retirement benefit, based on final average compensation and service as of the date of death, but without applying any reduction for the member's age at death.

There are optional forms of payment available on an actuarial equivalent basis. These include a life annuity payable while either the participant or the participant's beneficiary is alive, "popping-up" to the original life annuity if the beneficiary predeceases the member; a life annuity payable to the member while both the member and beneficiary are alive, reducing to 50 percent of this amount if the member predeceases the beneficiary, and "popping-up" to the original life annuity if the beneficiary predeceases the member; a life annuity payable to the member, with a guarantee that, should the member die prior to receiving 60 payments, the payments will be continued to a beneficiary for the balance of the five-year period; a life annuity payable to the member, with a guarantee that, should the member die prior to receiving 240 payments, the payments will be continued to a beneficiary for the balance of the 20-year period; a life annuity payable to the member, with a guarantee that, should the member die prior to receiving 120 payments, the payments will be continued to a beneficiary for the balance of the 10-year period; or a nonlevel annuity payable to the member, designed to provide a level total income when combined with the member's Social Security benefit. The option to receive a life annuity payable to the member with a guarantee that, should the member die prior to receiving 60 payments, the benefits will be continued to a beneficiary for the balance of the five-year period is not available to employees who retire on or after August 1, 2003. Retirees who elected this option before August 1, 2003, are not affected. In addition, members may elect a partial lump sum option at retirement. Under this option, a member receives an immediate lump sum equal to 12 times the monthly life annuity benefit and a reduced annuity. The reduction is determined actuarially. The member can then elect to receive the annuity benefit in one of the other optional forms, except that members who receive a partial lump sum option may not elect the level income option. The partial lump sum option is not available to disabled retirees or retirees who are not eligible for an unreduced retirement benefit. Actuarial equivalencies are based on tables adopted by the board of trustees.

The following chart provides a recent history of TFFR retirement plan changes:

July 1	Plan Improvements	Benefit Formula Increase	Retired Member Increase	Amount Average Increase	Average Increase Percentage	Average Monthly Benefits
1991	Provisions for military service credit under Veterans' Reemployment Rights Act (VRRA) added	Multiplier increased to 1.39% (final average salary (FAS) x 1.39% x years of service)	10% of current benefit or leveling benefit increase based on retirement date and years of service (maximum of $75/month)	$63.24	14.66%	1990 - $415 1991 - $513
1993	Disability retirement formula changed to coin-cide with retirement formula	Multiplier increased to 1.55% (FAS x 1.55% x years of service)	10% of current benefit or leveling benefit increase based on retirement data and years of service (maximum of $100/month)	$75.00	13.80%	1992 - $549 1993 - $547
1995	Allow members to roll over refunds from TFFR to IRA or qualified plan	No change	No increase	$0	0%	1994 - $663 1995 - $690
1997	Employer and employee contributions increased to 7.75% Allow rollovers to purchase service credit Expand TFFR Board to 7 members	Multiplier increased to 1.75% (FAS x 1.75% x years of service)	$30 per month increase	$30.00	4.1%	1996 - $719 1997 - $729
1999	Vesting and eligibility for benefits reduced from 5 to 3 years Early retirement reduction changed from age 65 to earlier of age 65 or Rule of 85 Purchase of service credit modified; air time and leave of absence added Member's spouse required to be beneficiary and spousal consent to choice of benefit option	Multiplier increased to 1.88% (FAS x 1.88% x years of service)	Increase equal to $2 per month x member's years of service credit + $1 per month x number of years since member's retirement	$70.00	8.5%	1998 - $810 1999 - $833
2001	Modified retiree employ-ment provisions by adding exceptions for critical shortage areas and educational foundation donations, and improved	Multiplier increased to 2.00% (FAS x 2.00% x years of service)	Increase equal to $2 per month x member's years of service credit + $1 per month x number of years since member's retirement + 0.75% annual adjustment for 7/1/01 and 7/1/02	$78.00	7.8%	2000 - $970 2001 - $995

July 1	Plan Improvements	Benefit Formula Increase	Retired Member Increase	Amount Average Increase	Average Increase Percentage	Average Monthly Benefits
	recalculation of retiree benefits after returning to teach					
2003	Clarified definition of salary Updated dual-membership guidelines Added 20-year term certain and partial lump sum distribution (PLSO) options Expended refund and rollover options to purchase service credit Allow employers to purchase service credit on behalf of members	No change	No increase	$0	0%	2002 - $1,152 2003 - $1,203
2005	None	No change	No increase	$0	0%	2004 - $1,255 2005 - $1,309

Retired Teachers Returning to Work

The committee received information on retired teachers returning to work. North Dakota law has, for many years, allowed retired teachers to return to work on a half-time basis or less. Although a few teachers have chosen this option in the past, in recent years, the committee learned more retired teachers are returning to work.

North Dakota Century Code Section 15-39.1-19.1 allows retirees of the Teachers' Fund for Retirement to return to teach and continue receiving their TFFR retirement benefits under one of the following options:

1. General rule - After a 30-day waiting period, a retiree may return to TFFR-covered employment for the following maximum number of hours in a fiscal year:

Nine-month contract	700 hours
Ten-month contract	800 hours
Eleven-month contract	900 hours
Twelve-month contract	1,000 hours

   Substitute teaching, extracurricular duties, and continuing professional development do not apply to the annual hour limit. No employer or employee retirement contributions are made to TFFR on behalf of the teacher under this option.

2. Exception A - Critical shortage area - A retiree may return to teaching in an approved critical shortage area and exceed the annual hour limitation without losing retirement benefits. If the retiree retired on or before January 1, 2001, no waiting period is required; however, if a retiree retired after January 1, 2001, a one-year waiting period is required. Critical shortage areas are determined each year by the Education Standards and Practices Board. The committee learned the board primarily determines critical shortage areas based upon the ratio of regularly licensed teachers in the state who are qualified for the position to the number of schools with open positions requesting alternative access licensure. In cases where near shortages exist, the board gives additional consideration to whether the hiring school has made a diligent effort to attract and hire regularly licensed teachers. For the 2005-06 school year, the board designated all teaching areas, except elementary education and physical education, as critical shortage areas in the state. No employer or employee retirement contributions are made to TFFR on behalf of the teacher under this option.
3. Exception B - Benefit suspension and recalculation - After a 30-day waiting period, a retiree may return to TFFR-covered employment and exceed the annual hour limitation; however, retirement benefits will be suspended the first of the month following the month the retiree reaches the annual hour limit. At that time, the employer and employee contributions must be paid on any salary earned after the annual hour limit based on the employer's TFFR payment model. Once the retiree again retires, monthly benefits are recalculated.

The following schedule shows the number of retirees who have returned to work for the 1999-2000 school year compared to the 2005-06 school year.

	1999-2000	2005-06
Number of retirees returning to teaching	26	160
Superintendents/administrators	9	48
Teachers	17	112
General rule	24	151
Critical shortage area	0	6
Suspend and recalculate	2	3
Average age	62	60
Average salary	$13,000	$22,000

The committee learned North Dakota school districts employed 181 first-year teachers for the 2003-04 school year, 200 for the 2004-05 school year, and 190 for the 2005-06 school year.

The committee heard testimony from other interested persons and learned that it is important for school districts to have the ability to hire part-time teachers as the number of students declines, especially in rural areas of the state where it is difficult to recruit part-time teachers.

Actuarial Report

The latest available report of the consulting actuary was dated July 1, 2006. The primary purposes of the valuation report are to determine the adequacy of the current employer contribution rate, to describe the current financial condition of the Teachers' Fund for Retirement, and to analyze changes in the fund's condition. In addition, the report provides information required by the Teachers' Fund for Retirement in connection with Governmental Accounting Standards Board (GASB) Statement No. 25 and provides various summaries of the data. Valuations are prepared annually, as of July 1 of each year, the first day of the Teachers' Fund for Retirement's fiscal year.

The 2006 Teachers' Fund for Retirement actuarial report indicates:

- The number of active members in TFFR in 2006 was 9,585, a reduction of 216 or 2.2 percent from the number of active members in 2005 of 9,801. The reduction is partially due to new procedures used in the new TFFR computer data system which counts members who retire on July 1 of each year as a retiree rather than as an active member.
- Over the last 10 years, active membership in the fund has decreased by an average of .2 percent per year.
- There are 1.6 active members in TFFR for each retiree compared to 2.2 active members for each retiree 10 years ago.
- The number of retirees in 2006 increased by 307 or 5.5 percent, from 5,586 in 2005 to 5,893 in 2006. The average annual retiree benefit is $16,595.
- Payroll for 2006 for active members increased by .9 percent, from $386.6 million to $390.1 million, compared to an average increase of 3.3 percent per year over the last 10 years.
- Average active member pay increased by 3.2 percent, from $39,447 per year to $40,703 per year.
- The fair market value of the fund's assets increased from $1.53 billion in fiscal year 2005 to $1.72 billion in fiscal year 2006.
- Total contributions were $65.6 million for fiscal year 2006 compared to $64.1 million for fiscal year 2005.
- Total distributions in fiscal year 2006 were $96 million, compared to $89.3 million in fiscal year 2005.

The Government Accounting Standards Board Statement No. 25 provides a guide for determining required contribution rates for retirement funds. The actual employer contribution to the fund is 7.75 percent. When calculating the annual required employer contribution based on the GASB statement, the contribution for fiscal year 2006 should have been 12.12 percent. The difference of 4.37 percent is referred to as "negative margin." The committee learned that the TFFR Board of Trustees, in 2005, changed the factors used in calculating the GASB annual required contribution from amortizing the unfunded liability of the plan using a level payroll over 20 years to assuming 2 percent annual payroll increases with an amortization period of 30 years.

Actual investment returns for recent years have been:

- Fiscal year 2002 - (8.6 percent),
- Fiscal year 2003 - 2.1 percent,
- Fiscal year 2004 - 18.9 percent,
- Fiscal year 2005 - 13.3 percent, and
- Fiscal year 2006 - 14.6 percent.

The average return over the last 10 years has been 8.3 percent, which is .3 percent more than the assumed investment return rate of 8 percent. Investment returns are averaged over a five-year period when determining "actuarial" asset value.

The unfunded actuarial accrued liability of the fund increased from $495.5 million in 2005 to $509.9 million in 2006. Over the same time period the funded ratio based on actuarial value increased from 74.8 to 75.4 percent. Using the market value of the fund's assets, the funded ratio would be 83 percent.

Assuming the fund earns 8 percent in future years, the committee learned the unfunded liability of the Teachers' Fund for Retirement is estimated to increase from its current level of $509.9 million to $947.3 million in 30 years.

The major reasons the fund's financial condition has decreased from a 102 percent funding ratio in 2000 to a 75 percent funding ratio for 2006 are the result of:

- Lower investment returns during 2001 through 2003.
- Changes in actuarial assumptions reflecting larger salary increases, longer life expectancies fewer members leaving the fund before retirement, and members retiring earlier.
- Benefit improvements authorized in 2001, when the formula multiplier increased from 1.8 to 2 percent of final average salary.

Regarding the long-term stability of the fund, actuarial projections indicate that the fund will be able to pay all of its promised benefits for the next 30 years. Even in 2036, assuming 8 percent future earnings, assets are still projected to be more than 10 times annual distributions.

Proposals Affecting Teachers' Fund for Retirement

The following is a summary of proposals affecting TFFR which the committee took jurisdiction of and committee action on each:

Bill No. 73

Sponsor: State Board for Career and Technical Education

Proposal: Allows employees of the State Board for Career and Technical Education the option to transfer from TFFR to PERS. For those employees who make the transfer, TFFR would move the employees service, account balance, and pay and contribution history to PERS and PERS would be responsible for any benefits due based on each employee's service. The bill also allows future employees hired by the State Board for Career and Technical Education to elect to join PERS rather than TFFR.

Actuarial Analysis: 16 employees of the State Board for Career and Technical Education who are members of TFFR would be eligible to make the transfer. As of June 30, 2006, the average age for the group was 53, the average years of service was 20, and the average salary of the employees was $49,337 per year.

The actuarial analysis determined the asset transfer amount would be $2,897,301 from TFFR to PERS for these employees if they all make the transfer.

The actuarial analysis indicates that if the bill is approved, and all eligible employees transfer to PERS, TFFR will be "worse off" by $235,766, the unfunded actuarial liability will increase by $38,906, and the annual required contribution based on GASB Statement No. 25 for fiscal year 2007 would increase from 12.29 to 12.31 percent.

Committee Report: No recommendation.

Bill No. 68

Sponsor: TFFR Board of Trustees

Proposal: Major provisions of the bill draft:

1. Incorporate federal tax law changes to comply with Internal Revenue Service requirements.
2. Increase employer retirement contribution rates by 1 percent, from 7.75 to 8.75 percent of active members' salaries. The employee contribution remains at 7.75 percent.
3. Require employer contributions of 16.5 percent of a reemployed retiree's salary.
4. Provide that if a member elects a refund, the member waives any right to participate in the fund under the same membership provisions that existed when the refund was taken.
5. Create a new tier (Tier II) of reduced member benefits for TFFR members employed on or after July 1, 2007, by:
    a. Modifying normal retirement benefit eligibility for new members (Tier II) to age 65 and five years of service or the Rule of 90 rather than the eligibility for current members (Tier I) of age 65 and three years of service or the Rule of 85.
    b. Modifying the final average salary calculation for new members (Tier II) to provide for a five-year final average salary calculation rather than the three-year final average salary calculation for current members (Tier I).
    c. Modifying the vesting schedule for new members (Tier II) to five years of service rather than the vesting schedule of three years of service for current members (Tier I).
    d. Modifying the early retirement eligibility for new members (Tier II) to age 55 and five years of service rather than age 55 and three years of service for current members (Tier I).
    e. Modifying the employer service purchase conditions for new members (Tier II) to age 55 and five years of service and a Rule of 82 rather than age 55 and three years of service with a Rule of 77 for current members (Tier I).

The committee amended the bill at the request of the TFFR Board of Trustees to provide a $5,000 special funds appropriation from the Teachers' Fund for Retirement to pay administrative costs to implement provisions of the bill.

Actuarial Analysis: The following chart compares TFFR without provisions of Bill No. 68 and with provisions of Bill No. 68, as amended, over 10 and 30 years. The projections are based on current actuarial assumptions, including an 8 percent net investment return and active membership declining by .5 percent per year.

Item	July 1, 2006, Current Valuation	July 1, 2016, No Changes	July 1, 2016, With Bill No. 68
Funded ratio	75.4%	84.0%	86.0%
Unfunded actuarial accrued liability	$509.9 million	$482.5 million	$420.5 million
Annual required contribution	12.29%	10.17%	8.28%
Margin[1]	-4.54%	-2.42%	0.47%
Funding period[2]	Infinite	Infinite	24.8 years
Item	**July 1, 2006, Current Valuation**	**July 1, 2036, No Changes**	**July 1, 2036, With Bill No. 68**
Funded ratio	75.4%	82.4%	100.4%
Unfunded actuarial accrued liability	$509.9 million	$947.3 million	-$20.1 million
Annual required contribution	12.29%	10.35%	2.37%
Margin[1]	-4.54%	-2.60%	6.38%
Funding period[2]	Infinite	Infinite	0.0 years

[1]The margin is the difference between the statutory contribution rate and GASB's annual required contribution. It is the result of subtracting the annual required contribution from 7.75% (or 8.75% under Bill No. 68). A negative margin represents a shortfall and a positive margin indicates the statutory contribution is sufficient.

[2]The funding period is the theoretical number of years required to amortize the unfunded accrued actuarial liability using the statutory contribution rate.

Committee Report: Favorable recommendation.

Bill No. 67

Sponsor: Representative Matthew M. Klein

Proposal: Reduces the number of hours a retired member of TFFR may work each year and continue to receive retirement benefits and limits the areas in which a retired member of TFFR may return to teach under the "critical shortage area" to only mathematics and science.

Actuarial Analysis: Provisions of the bill are estimated to potentially reduce the GASB annual required contribution by .38 percent, from 12.29 to 11.91 percent in 2007. The unfunded actuarial accrued liability would decrease by about $15 million and the funded ratio would improve from 75.4 to 76 percent.

Committee Report: No recommendation because the bill was withdrawn by the sponsor.

PUBLIC EMPLOYEES RETIREMENT SYSTEM

Programs

The Public Employees Retirement System is governed by NDCC Chapter 54-52 and includes the Public Employees Retirement System main system, judges' retirement system, National Guard retirement system, law enforcement with prior main service, law enforcement without prior main service, and an optional defined contribution retirement plan; Highway Patrolmen's retirement system; Job Service North Dakota retirement plan; and retiree health benefits fund. The Public Employees Retirement System is supervised by the Retirement Board and covers most employees of the state, district health units, and the Garrison Diversion Conservancy District. Elected officials and officials first appointed before July 1, 1971, can choose to be members. Officials appointed to office after that date are required to be members. Most Supreme Court and district court judges are members of the plan but receive benefits that are different from benefits received by other members. A county, city, or school district may choose to participate on completion of an employee referendum and on execution of an agreement with the Retirement Board. Political subdivision employees are not eligible to participate in the defined contribution retirement plan. The Retirement Board also administers the uniform group insurance, life insurance, flexible benefits, deferred compensation, and Chapter 27-17 judges' retirement programs. The Chapter 27-17 judges' retirement program is being phased out of existence except to the extent its continuance is necessary to make payments to retired judges and their surviving spouses and future payments to judges serving on July 1, 1973, and their surviving spouses as required by law.

Contribution Rates and Benefits

Main System

The contribution rate for members of the main system is 4 percent and the employer contribution is 4.12 percent. A part-time employee in the main system contributes 8.12 percent with no employer contribution. The contribution rates are set in statute.

A member of the main system is eligible for normal service retirement benefits at age 65 or when age plus years of service is equal to at least 85--the Rule of 85. The retirement benefit is 2 percent of the final average salary multiplied by years of service. Final average salary is the average of the highest salary received by the member for any 36 consecutive months employed during the last 120 months of employment.

A member of the main system is eligible for an early service retirement at age 55 with three years of service. The retirement benefit for a member who elects early service retirement is the normal service retirement; however, a benefit that begins before age 65, or Rule of 85, if earlier, is reduced by one-half of 1 percent for each month before the earlier of age 65 or the age at which the Rule of 85 is met.

A member of the main system with six months of service who is unable to engage in any substantial and gainful activity is eligible for a disability benefit of 25 percent of the member's final average salary at disability with a minimum of $100 per month.

A member of the main system is eligible for deferred vested retirement at three years of service. The deferred vested retirement is the normal service retirement benefits payable at age 65 or the Rule of 85 if earlier. Reduced early retirement benefits may be elected upon attainment of age 55.

The surviving spouse of a deceased member of the main system who accumulated at least three years of service before normal retirement is entitled to elect one of four forms of preretirement death benefits. The preretirement death benefit may be a lump sum payment of the member's accumulated contribution with interest; the member's accrued benefit payable for 60 months to the surviving spouse; 50 percent of the member's accrued benefit, not reduced on account of age, payable for the surviving spouse's lifetime; or continuation portion of a 100 percent joint and survivor annuity, only available if the participant was eligible for normal retirement.

Defined Contribution Plan

Under the main retirement system, certain employees are eligible to participate in a defined contribution plan. Pursuant to Chapter 54-52.6, a permanent state employee, except an employee of the Judicial Branch or an employee of the State Board of Higher Education and state institutions under the jurisdiction of the board, who is in a position not classified by Human Resource Management Services of the Office of Management and Budget may elect to participate in the defined contribution retirement plan.

The defined contribution plan allows a participating employee to control the investment of funds in the employee's own retirement account into which the employee and state contributions are deposited. Retirement benefits are dependent upon the employee's account value at retirement.

National Guard Retirement System

The contribution rate for a member of the National Guard retirement system is 4 percent, and the employer contribution is 8.33 percent. The employee contribution rate is set in statute; however, the employer contribution rate is not.

A member of the National Guard retirement system is eligible for a normal service retirement at age 55 and three consecutive years of service. The retirement benefit of the National Guard retirement system is 2 percent of the final average salary multiplied by years of service. Final average salary is the average of the highest salary received by the member for 36 consecutive months employed during the last 120 months of employment.

A member of the National Guard retirement system is eligible for early service retirement at age 50 with three years of service. The early service retirement benefit for a member of the National Guard retirement system is the normal service retirement benefit; however, a benefit that begins before age 55 is reduced by one-half of 1 percent for each month before age 55.

A member of the National Guard retirement system with six months of service who is unable to engage in any substantial gainful activity is eligible for a disability benefit of 25 percent of the member's final average salary with a minimum of $100 per month.

A member of the National Guard retirement system is eligible for deferred vested retirement at three years of service. The deferred vested retirement benefit for the National Guard retirement system is the normal service retirement benefit payable at age 55. Reduced early retirement may be elected upon attainment of age 50.

The surviving spouse of a deceased member of the National Guard who had accumulated at least three years of service before normal retirement is entitled to elect one of four forms of preretirement death benefits. The preretirement death benefit may be a lump sum payment of the member's accumulated contribution with interest; the member's accrued benefit payable for 60 months to the surviving spouse; 50 percent of the member's accrued benefit, not reduced on account of age, payable for the surviving spouse's lifetime; or continuation portion of a 100 percent joint and survivor annuity, only available if the participant was eligible for normal retirement.

Law Enforcement Retirement Systems

The law enforcement retirement system is available to correctional or peace officers of political subdivisions that choose to participate in the PERS retirement system. State agency employees are not eligible to participate in the law enforcement retirement system.

The contribution rate for a member of the law enforcement retirement system with prior main service is 4 percent, and the employer contribution is 8.31 percent. The contribution rate for a member of the law enforcement retirement system without prior main service is 4 percent, and the employer contribution is 6.43 percent. The employee contribution rate is set in statute; however, the employer contribution is not.

A member of the law enforcement retirement system is eligible for a normal service retirement at age 55 and three consecutive years of service or when age plus service is equal to 85--Rule of 85. The retirement benefit for members of the law enforcement retirement system is 2 percent of final average salary multiplied by years of service. Final average salary is the average of the highest salary received by the member for any 36 consecutive months employed during the last 120 months of employment.

A member of the law enforcement retirement system is eligible for early service retirement at age 50 with three years of service. The early service retirement benefit for a member of the law enforcement retirement system is the normal service retirement benefit; however, a benefit that begins before age 55, or Rule of 85, if earlier, is reduced by one-half of 1 percent for each month before age 55.

A member of the law enforcement retirement system with six months of service who is unable to engage in any substantial gainful activity is eligible for a disability benefit of 25 percent of the member's final average salary at disability with a minimum of $100 per month.

A member of the law enforcement retirement system is eligible for deferred vested retirement at three years of service. The deferred vested retirement benefit for a member of the law enforcement retirement system is the normal service retirement benefit payable at age 50 or Rule of 85 if earlier. Reduced early retirement benefits may be elected upon attainment of age 50.

The surviving spouse of a deceased member of the law enforcement retirement system who had accumulated at least three years of service before normal retirement is entitled to elect one of four forms of preretirement death benefits. The preretirement death benefit may be a lump sum payment of the member's accumulated contribution with interest; the member's accrued benefit payable for 60 months to the surviving spouse; 50 percent of the member's accrued benefit, not reduced on account of age, payable for the surviving spouse's lifetime; or continuation portion of a 100 percent joint and survivor annuity only available if the participant was eligible for normal retirement.

The employee contribution rate for the law enforcement retirement system is specified by statute; however, the employer contribution rate is not.

Judges' Retirement System

The employee contribution rate for the judges' retirement system is 5 percent, and the employer contribution is 14.52 percent. These rates are set in statute.

The retirement benefit for a member of the judges' retirement system is 3.5 percent of final average salary for the first 10 years of service, 2.8 percent for each of the next 10 years of the service, and 1.25 percent for service in excess of 20 years. Final average salary is the average of the highest salary received by the member for any 36 consecutive months employed during the last 120 months of employment.

A member of the judges' retirement system is eligible for early service retirement at age 55 with five years of service. The early service retirement benefit for a member of the judges' retirement system is the normal service retirement; however, a benefit that begins before age 65, or Rule of 85, if earlier, is reduced by one-half of 1 percent for each month before age 65.

A member of the judges' retirement system with six months of service who is unable to engage in any substantial gainful activity is eligible for a disability benefit of 70 percent of the member's final average salary at disability minus Social Security and workers' compensation benefits paid.

A member of the judges' retirement system is eligible for deferred vested retirement at five years of service. The deferred vested retirement benefit is the normal service retirement benefit payable at age 65 or the Rule of 85, if earlier. Reduced early retirement benefits may be elected upon attainment of age 55.

The surviving spouse of a deceased member of the judges' retirement system who would have accumulated at least five years of service is entitled to elect one of two forms of preretirement death benefits. The preretirement death benefit may be a lump sum payment of the member's accumulated contribution or 100 percent of the member's accrued benefit not reduced on account of age, payable for the spouse's lifetime.

Highway Patrolmen's Retirement System

The contribution rate for a member the Highway Patrolmen's retirement system is 10.3 percent, and the employer contribution is 16.7 percent. These rates are set in statute.

A member of the Highway Patrolmen's retirement system is eligible for a normal service retirement at age 55 with at least 10 years of eligible employment or with age plus service equal to at least 80--the Rule of 80. The normal service retirement benefit is 3.6 percent of final average salary for the first 25 years of service and 1.75 percent for service in excess of 25 years. Final average salary is the highest salary received by the member for any 36 consecutive months employed during the last 120 months of employment.

A member is eligible for early service retirement at age 50 with 10 years of eligible retirement. The early service retirement benefit is a normal service retirement benefit; however, a benefit that begins before age 55, or Rule of 80, if earlier, is reduced by one-half of 1 percent for each month before age 55.

A member is eligible for a disability benefit at six months of service and an inability to engage in substantial gainful activity. The disability benefit is 70 percent of the member's final covered salary at disability less workers' compensation, with a minimum of $100 per month.

A member is eligible for deferred retirement benefit upon 10 years of eligible employment. The deferred retirement benefit is a normal service retirement benefit payable at age 55 with a Rule of 80 if earlier. Vested benefits are indexed at a rate set by the retirement board based upon the increase of the final average salary from the date of termination to the benefit commencement date. Reduced early retirement benefits may be elected upon attainment of age 50.

Preretirement death benefits are available to a surviving spouse of a deceased member of the Highway Patrolmen's retirement system who had accumulated at least 10 years of service in one of the three forms--a lump sum payment of accumulated contributions with interest; monthly payment of the member's accrued benefit for 60 months; or 50 percent of the member's accrued benefit, not reduced on account of age, for the surviving spouse's lifetime. If the deceased member had accumulated less than 10 years of service, or if there is no surviving spouse, then a death benefit equal to the member's accumulated contributions with interest calculated at 7.5 percent is paid in a lump sum.

The normal form of benefit for the Highway Patrolmen's retirement system is a monthly benefit for life with 50 percent of the benefit continuing for the life of the surviving spouse, if any. Optional forms of payment are a 100 percent joint and surviving annuity, 5-year certain and life annuity, and 10-year certain and life annuity.

Job Service North Dakota Retirement Plan

The PERS Board assumed administration of the Job Service North Dakota retirement plan from Job Service North Dakota pursuant to the legislation enacted in 2003. It is a closed retirement plan for employees of Job Service North Dakota.

Employer "Pickup" Provision

During the 1983-85 biennium, the state implemented the employer "pickup" provision of the Internal Revenue Service Code allowing a portion or all of the required employee contributions to be made by the employer. The state chose, in lieu of a salary increase during this biennium, to pay employee contributions of 4 percent.

Portability Enhancement Provision

Effective January 1, 2000, a PERS member's account balance includes vested employer contributions equal to the member's contribution to the deferred compensation program under NDCC Chapter 54-52.2. The vested employer contribution may not exceed $25 or 1 percent of the member's salary, whichever is greater, for months 1 through 12 of service credit; $25 or 2 percent of the member's monthly salary, whichever is greater, for months 13 through 24 of service credit; $25 or 3 percent of the member's monthly salary, whichever is greater, for months 25 through 36 of service credit; and $25 or 4 percent of the member's monthly salary, whichever is greater, for service exceeding 36 months. The vested employer contributions may not exceed 4 percent of the member's monthly salary and are credited monthly to the member's account balance. The fund can accept rollovers from other qualified plans under rules adopted by the Retirement Board for purchase of additional service credit.

Members Terminating Employment

In lieu of a monthly retirement benefit, terminating nonvested members and terminating vested members of the main system, National Guard retirement system, law enforcement retirement system, and judges' retirement system may elect to receive accumulated member contributions with interest. Member contributions through June 30, 1981, accumulate with interest of 5 percent, member contributions from July 1, 1981, through June 30, 1986, accumulate with interest of 6 percent, and member contributions after June 30, 1986, accumulate with interest of .5 percent less than the actuarial interest rate assumption. The standard form of payment is a monthly benefit for life with a refund to the beneficiary at death of the remaining balance, if any, of accumulated member contributions. Optional forms of payment are a 50 percent joint and surviving annuity; 100 percent joint and survivor annuity with "popup" feature; 5-year certain and life annuity; 10-year certain and life annuity; or a level Social Security income annuity. The standard form of payment for members of the judges' retirement system is a monthly benefit for life, with 50 percent payable to an eligible survivor. In addition to the optional forms of payment available to members of the main system, National Guard, and law enforcement retirement systems, a member of the judges' retirement system may elect to receive a life annuity.

Multiplier and Retiree Adjustments

The following schedule shows the multiplier percentages and benefit adjustments since 1977:

Date	Multiplier	Benefit Adjustment
7/77	1.04%	1.04%
7/83	1.20%	15.38%
7/85	1.30%	8.33%
7/87	1.50%	15.38%
7/89	1.65%	15.76%
7/91	1.69%	2.42%
8/93	1.725%	2.00%
1/94	1.74%	1.00%
8/97	1.77%	5.00%
8/99	1.89%	8.00%
8/01	2.00%	6.00%
In 2006 there will be a 13th check equal to half the monthly payment.		

Retiree Health Credit

In 1989 the Legislative Assembly established a retiree health insurance credit fund account with the Bank of North Dakota with the purpose of prefunding hospital benefits coverage and medical benefits coverage under the uniform group insurance program for retired members of the Public Employees Retirement System and the Highway Patrolmen's retirement system receiving retirement benefits or surviving spouses of those retired members who have accumulated at least 10 years of service. The employer contribution under the Public Employees Retirement System was reduced from 5.12 to 4.12 percent, under the judges' retirement system from 15.52 to 14.52 percent, and under the Highway Patrolmen's retirement system from 17.07 to 16.07 percent or 1 percent of the monthly salaries and wages of participating members, including participating Supreme Court and district court judges, and the money was redirected to the retiree health insurance credit fund. Upon retirement, an employee will receive a credit of $4.50 per month for each year of service of the employee which will reduce the monthly health insurance premium.

Retiree Health Insurance

The committee reviewed information regarding prescription drug coverage for retirees of the Public Employees Retirement System after implementation of the Medicare Part D prescription drug benefit. The committee learned the PERS board, effective January 1, 2006, began providing prescription drug coverage for its retirees through a prescription drug plan offered by Blue Cross Blue Shield of North Dakota. This plan will maximize federal support for prescription drug coverage for these retirees. The formulary offered by Blue Cross Blue Shield will be slightly more restrictive than the current formulary. The out-of-pocket maximum for prescription drugs increased from $1,000 to $3,000 per year; however, the monthly health insurance premium decreased by 10 to 20 percent effective January 1, 2006.

Retirements

The committee reviewed information included in the following chart regarding the number of state employee retirements and projected retirements:

Fiscal Year	Actual	Fiscal Year	Projected
2001	319	2007	468
2002	305	2008	507
2003	399	2009	560
2004	339	2010	604
2005	374		
2006	429		

Legal Issues of Retirement Benefit Changes

The committee received information from the Attorney General's office on legal issues relating to retirement benefit changes for current employees and retirees. The committee learned both the federal and state constitutions include a contract clause providing that a state cannot pass a law impairing a contractual obligation. Public pension obligations in North Dakota are contractual obligations. In addition, North Dakota Century Code Section 54-52-14.3 provides that any provision of law relating to the use and investment of public employee retirement funds must be deemed a part of the employment contracts of the employees participating in any public employee retirement system.

The Attorney General's office believes the North Dakota Supreme Court would follow the "California Rule" which provides that a governing body may make plan changes, but any changes that disadvantage an employee must be accompanied by comparable advantageous changes.

There are four membership designations in public pension plans--retirees, inactives, actives, and future actives. Based on the Attorney General's legal research for retirees, no plan changes may be made affecting current retirees' pension benefits. For inactive members, the benefits that the inactives have already accrued cannot be detrimentally changed; however, since the employment contract has been terminated, there is no restriction on the state's ability to make modifications to the benefit structure available to vested inactives upon their future reemployment. Once they have been reemployed, the employment contract in effect on that date would control how future benefits accrue. For an active employee, under the "California Rule," the member's commencement of employment creates a contract that the state cannot unilaterally change to the member's detriment without a corresponding benefit; therefore, the state cannot detrimentally modify any provision of an active member's benefit structure without a corresponding benefit, including the Rule of 85, the vesting schedule, interest accrued to the member's account, the multiplier, and the amount of employee contribution. For future active employees, because there is no employment contract in place, the state can modify the plan to whatever extent it would like.

Alaska Pension Plan

The committee received information on the Alaska Public Employees Pension Plan. The Alaska pension plan provides retirement benefits based on an employee's average monthly salary for the highest 36 months of salary multiplied by 2 percent for the first 10 years of service, by 2.25 percent for the next 10 years of service, and by 2.5 percent for additional years of service. In addition, retirees receive full health insurance coverage as part of their retirement benefits.

The 2005 Alaska Legislature learned that the plan had an actuarial valuation of 75.2 percent and an unfunded liability of $5.7 billion. The Alaska Legislature learned that in order to address the unfunded liability, the employer contribution would need to increase from 11 percent to over 30 percent. As a result, the 2005 Alaska Legislature changed the retirement plan for employees hired on or after July 1, 2006, to a defined contribution plan and increased the employer contribution for current employees to 16 percent of salary.

Actuarial Report

The latest available report of the consulting actuary is dated July 1, 2006. The primary purpose of the valuation report is to determine the adequacy of the current employee contribution rate and to describe the current financial condition of the funds.

The following schedule presents the number of active members in each of the retirement plans:

Retirement Program	2005	2006
Main system	17,745	17,887
Highway Patrolmen's	125	127
Judges'	46	47
National Guard	14	41
Job Service North Dakota	52	44
Law enforcement with prior service	113	113
Law enforcement without prior service	13	14
Retiree health insurance credit fund	18,302	18,465

The main system and the Highway Patrolmen's retirement system had a 12.04 percent return on investment compared to the 2005 rate of return of 14.17 percent. The 10-year average rate of return on an actuarial valuation basis has been 8.53 percent. The goal for return on investment is 8 percent.

The following schedule presents the actuarial valuation of each of the retirement systems as of July 1, 2006:

Retirement Program	Actuarial Value of Assets	Actuarial Value of Liabilities	Surplus (Unfunded) Actuarial Accrued Liability
Main system	$1,286,478,642	$1,450,113,412	($163,634,770)
Highway Patrolmen's	$42,758,360	$49,127,046	($6,368,686)
Judges'	$23,283,465	$21,657,761	$1,625,704
National Guard	$1,583,896	$1,561,329	$22,567
Job Service North Dakota	$70,628,705	$69,967,001	$661,704
Law enforcement with prior service	$3,123,735	$7,001,165	($3,877,430)
Law enforcement without prior service	$73,167	$123,034	($49,867)
Retiree health insurance fund	$34,020,413	$82,632,628	($48,612,215)

The following schedule shows the actuarial funding ratio for each of the retirement programs for recent years:

Retirement Program	2002	2003	2004	2005	2006
Main system	104%	98%	94%	91%	89%
Highway Patrolmen's	97%	93%	90%	88%	87%
Judges'	122%	115%	113%	109%	108%
National Guard	139%	126%	120%	108%	101%
Job Service North Dakota	113%	109%	109%	109%	101%
Law enforcement with prior service			87%	41%	45%
Law enforcement without prior service			109%	48%	59%
Retiree health insurance credit fund	38%	38%	38%	39%	41%

The following schedule shows the annual required contribution (ARC) rates for 2005 and 2006 based on GASB guidelines, the statutory contribution rate, and the margin for 2006:

Retirement Program	2005 ARC Rate	2006 ARC Rate	2006 Statutory Rate	2006 Margin
Main system	6.03%	6.90%	4.12%	(2.78%)
Highway Patrolmen's	17.61%	19.03%	16.70%	(2.33%)
Judges'	11.62%	12.36%	14.52%	2.16%
National Guard	1.58%	4.02%	6.50%	2.48%
Job Service North Dakota	N/A	N/A	N/A	N/A
Law enforcement with prior service	12.03%	12.07%	8.31%	(3.76%)
Law enforcement without prior service	7.61%	7.43%	6.43%	(1.00%)
Retiree health insurance credit fund	1.00%	1.00%	1.00%	0%

Proposals Affecting Public Employees Retirement System

The following is a summary of the proposals affecting PERS which the committee took jurisdiction of and the committee's action on each proposal:

Bill No. 75

Sponsor: PERS Board

Proposal: Provides a retiree of the PERS defined benefit retirement plan or the Highway Patrolmen's retirement system is to receive an additional **one-time payment** equal to 75 percent of the retiree's monthly retirement benefit in either January 2008 or January 2009 if the total return on the fund is 9.16 percent or more in the preceding actuarial report. A retiree of the judges' retirement system is to receive a payment adjustment of 2 percent of their retirement benefit in January 2008 and January 2009. These increases will be paid only if PERS determines there is sufficient actuarial margin to pay for the increases.

The committee amended the bill at the request of the PERS Board to reduce the return on investment from 9.16 to 9.06 percent in accordance with the actuarial analysis.

Actuarial Analysis: The consulting actuary reported the return on investment target to provide for the one-time payment could be adjusted from 9.16 to 9.06 percent.

Under the judges' retirement system, the actuarial analysis indicates the 2 percent benefit increase for each year of the biennium would cost .46 percent of payroll. Since the judges' retirement system has a margin of 2.16 percent, the actuarial analysis indicated the increase would be affordable.

Committee Report: No recommendation.

Bill No. 76

Sponsor: PERS Board

Proposal: Includes technical corrections to the calculation of final average salary, allows an alternate payment method for those who delay taking retirement benefits after the normal retirement date, updates federal compliance provisions, and makes technical changes to sick leave conversion provisions.

The committee amended the bill at the request of the PERS Board to limit purchase of service options to active contributing members and to provide that members participating in the defined contribution plan who have less than four years of service will fully vest at age 65.

Actuarial Analysis: The actuarial analysis indicates the proposal has no actuarial impact.

Committee Report: Favorable recommendation.

Bill No. 80

Sponsor: PERS Board

Proposal: Provides for a 2 percent increase in retirement benefits to retirees of the Public Employees Retirement System and the Highway Patrolmen's retirement system in August 2009 and fully pays for the increase over two years by increasing the employer contribution under the Highway Patrolmen's retirement system by 5 percent, from 16.7 to 21.7 percent, and the Public Employees Retirement System by 1 percent, from 4.12 to 5.12 percent. The bill draft becomes effective August 1, 2009.

The committee amended the bill at the request of the PERS Board to reduce the employer contribution increase effective August 2009 from 1 to .64 percent for the main retirement system and from 4.37 to 3.95 percent for the Highway Patrolmen's retirement system.

Actuarial Analysis: Based on a two-year amortization schedule, the actuarial cost of the bill, as amended, would be .64 percent of payroll for the main retirement system, .36 percent of payroll for the National Guard retirement system, and 3.95 percent of payroll for the Highway Patrolmen's retirement system. The employer contribution increases are estimated to cost state agencies and higher education institutions $4.6 million per biennium, of which $1.9 million is from the general fund.

Committee Report: No recommendation.

Bill No. 77

Sponsor: PERS Board

Proposal: Provides for an automatic enrollment process for new employees in the deferred compensation program at $25 per month unless the employee elects not to participate.

Actuarial Analysis: The actuarial analysis indicates the proposal has no actuarial impact.

Committee Report: Favorable recommendation.

Bill No. 79

Sponsor: PERS Board

Proposal: Provides for an increase in the monthly retiree health credit from $4.50 per year of credited service to $5 per year of credited service and pays for the increase by increasing the retiree health credit employer contribution by .15 percent, from 1 to 1.15 percent of payroll.

Actuarial Analysis: The actuarial impact on the retiree health benefit fund is .15 percent of payroll. The estimated cost of increasing employer contributions by .15 percent for a biennium for state agencies and higher education institutions is $980,000, of which $354,000 is from the general fund.

Committee Report: No recommendation.

Bill No. 71

Sponsor: Senator Karen K. Krebsbach

Proposal: Authorizes employees of the North Dakota Association of Counties to participate in the Public Employees Retirement System, the retiree health benefits fund, the uniform group insurance program, and the deferred compensation program.

The committee amended the bill at the request of the North Dakota Association of Counties to clarify that the Association of Counties is an instrumentality of government.

Actuarial Analysis: The actuarial analysis indicates the bill, as amended, has no actuarial impact on the retirement system.

Committee Report: Favorable recommendation.

Bill No. 78

Sponsor: PERS Board

Proposal: Creates a tax-exempt trust into which an employee's unused annual leave and 10 percent of the employee's unused sick leave would be deposited into and used for qualified health care expenses during the employee's retirement; increases the term life insurance policy provided for employees from a minimum of $1,000 to a minimum of $5,000; allows a separate prescription drug plan to be provided for retirees due to the establishment of the federal Medicaid Part D prescription drug program; allows the retiree health credit for employees and spouses, who are also state employees, to be combined; requires temporary employees to work a minimum of 20 hours per week and at least 20 weeks per year to be eligible to participate in the uniform group insurance program; and allows a temporary employee's employer to determine whether the temporary employee or the employer will pay the monthly premium for the health insurance coverage.

The committee amended the bill at the request of the PERS Board to remove provisions relating to the creation of a trust into which an employee's unused annual leave and 10 percent of the employee's unused sick leave would be deposited into and used for qualified health care expenses during the employee's retirement. These sections were removed because federal law does not allow employees to choose to withdraw mandatory payments from the trust in cash.

Actuarial Analysis: The actuarial analysis indicates most of the provisions in the bill, as amended, are cost-neutral. Increasing the term life insurance policies from $1,000 to $5,000 is estimated to cost state agencies and higher education institutions approximately $280,000 per biennium, of which $61,000 is from the general fund.

Committee Report: Favorable recommendation.

Bill No. 62

Sponsor: Representative Clara Sue Price

Proposal: Authorizes public health districts and the Garrison Diversion Conservancy District to participate in the uniform group insurance program under the same terms and conditions as state agencies. The proposal will allow the public health districts to continue to pay the blended premium rate similar to state agencies rather than the separate single rate and family rate paid by other political subdivisions.

The committee amended the bill at the request of the PERS Board to require these districts to participate under the same terms and conditions as a state agency rather than making it optional.

Actuarial Analysis: The actuarial analysis indicates that, at current premium rates, if all public health units were required to pay the separate political subdivision single/family rates, PERS will collect an estimated additional $218,000 per year in premiums.

Committee Report: Favorable recommendation.

Bill No. 30

Sponsor: Senator Tim Mathern

Proposal: Expands the uniform group insurance program to allow participation by members of the North Dakota National Guard.

Actuarial Analysis: The actuarial analysis indicates that expanding eligibility could result in adverse selection that may increase plan costs. However, Section 7 of the bill mitigates this concern by providing the PERS Board authority to not implement the bill unless it can be done in a manner that will not impact the plan.

Committee Report: Unfavorable recommendation.

Bill No. 31

Sponsor: Senator Tim Mathern

Proposal: Expands the uniform group insurance program to allow participation by permanent employees of nonprofit organizations exempt from federal taxes under Section 501(c)(3) of the Internal Revenue Code.

Actuarial Analysis: The actuarial analysis indicates that expanding eligibility could result in adverse selection that may increase plan costs. Another concern identified is that the plan could lose its governmental status if nongovernmental employers are allowed. However, Section 7 of the bill mitigates these concerns by providing the PERS Board authority to not implement the bill unless it can be done in a manner that will not impact the plan.

Committee Report: Unfavorable recommendation.

Bill No. 32

Sponsor: Senator Tim Mathern

Proposal: Expands the uniform group insurance program to allow participation by permanent employees of private sector employers in the state employing 50 or fewer employees.

Actuarial Analysis: The actuarial analysis indicates that expanding eligibility could result in adverse selection that may increase plan costs. Another concern identified is that the plan could lose its governmental status if nongovernmental employers are allowed. However, Section 7 of the bill mitigates these concerns by providing the PERS Board authority to not implement the bill unless it can be done in a manner that will not impact the plan.

Committee Report: Unfavorable recommendation.

Bill No. 100

Sponsor: Senator Tim Mathern

Proposal: Expands the uniform group insurance program to allow participation by permanent employees of private sector employers in the state, by temporary employees of private sector employers, and to other residents of the state who do not have health insurance coverage through a private insurer or through a public benefits plan provided by a governmental entity.

Actuarial Analysis: The actuarial analysis indicates that expanding eligibility could result in adverse selection that may increase plan costs. Another concern identified is that the plan could lose its governmental status if nongovernmental employers are allowed. However, Section 7 of the bill mitigates these concerns by providing the PERS Board authority to not implement the bill unless it can be done in a manner that will not impact the plan.

Committee Report: Unfavorable recommendation.

Proposal Affecting the State Investment Board

The following is a summary of the proposal affecting the State Investment Board over which the committee took jurisdiction and the committee's action on the proposal:

Bill No. 82

Sponsor: State Investment Board

Proposal: Clarifies the investment powers of the State Investment Board.

The committee amended the bill at the request of the State Investment Board to provide specific statutory authority for the investment director of the State Investment Board to sign and execute all contracts and agreements relating to funds under the management of the board.

Actuarial Analysis: The State Investment Board reported that provisions of the bill, as amended, will have no actuarial impact to any of the funds invested by the State Investment Board nor will the Retirement and Investment Office incur any costs to implement provisions of the bill draft.

Committee Report: Favorable recommendation.

ADDITIONAL COMMITTEE RESPONSIBILITIES

The committee was not requested by the Public Employees Retirement System Board under NDCC Section 54-52.1-08.2 to approve terminology changes adopted by the Retirement Board to comply with federal requirements. The committee was not notified by any firefighters relief association pursuant to Section 18-11-15(5) that requires the Employee Benefits Programs Committee to be notified by a firefighters relief association if it implements an alternate schedule of monthly service pension benefits for members of the association.

Pursuant to NDCC Section 54-06-31, the committee received periodic reports from the director of Human Resource Management Services on the implementation, progress, and bonuses provided by state agency programs to provide bonuses to recruit or retain employees in hard-to-fill positions. The following schedule is a summary of the information presented:

	July 1, 2003, to June 30, 2005		July 1, 2005, to September 30, 2006	
Agency	**Recruitment (148 total)**	**Retention (31 total)**	**Recruitment (186 total)**	**Retention (0 total)**
Bank of North Dakota	$2,404.00	$41,400.34		
Department of Commerce			$2,000.00	
Department of Corrections and Rehabilitation	4,225.00		500.00	
Highway Patrol	2,250.00		3,500.00	
Department of Human Services	22,365.50	10,800.00	46,109.28	
Information Technology Department	15,550.00		14,900.00	
Job Service North Dakota	2,000.00			
Industrial Commission		20,000.00	300.00	
Department of Transportation	222,777.58		100,042.79	
Veterans Home	4,000.00			
Total	$275,572.08	$72,200.34	$167,352.07	$0

STATE EMPLOYEE COMPENSATION STUDY

The committee was assigned, pursuant to Section 28 of 2005 House Bill No. 1015, a study of issues relating to state employee compensation. The committee reviewed information relating to state employee compensation, including employee's compensation, salary increases, equity adjustments, retirement and health insurance benefits, and leave policies.

Background

Employees

The committee learned North Dakota state agencies were authorized to employ 10,631.95 full-time equivalent positions for the 2005-07 biennium. Of this total, 2,194.42 relate to higher education positions paid for with funding from the general fund, 743.65 to employees of the Agricultural Experiment Station, NDSU Extension Service, Upper Great Plains Transportation Institute, and Northern Crops Institute, and 7,693.88 relate to positions in all other agencies.

There are two types of state employees--classified and unclassified. Classified state employees are under the jurisdiction of the classification system administered by Human Resource Management Services, a division of the Office of Management and Budget (OMB). The classification system includes 20 pay grades. Each job title is assigned to a pay grade and each pay grade identifies the salary range that employees within that pay grade may be paid. There are approximately 6,400 classified state employees. All other employees are considered unclassified. Unclassified employees include elected and appointed officials and their deputies; employees of the legislative and judicial branches; employees of higher education; the Mill and Elevator, Workforce Safety and Insurance, and Department of Commerce; and physicians and teachers. The University System has its own system of categorizing employee positions called the "broadband" system.

Compensation

The committee learned state employee compensation consists of two components--salaries and fringe benefits. Except for elected officials, whose salaries are set in state statute, all other state employee salary levels are set by the governing body or supervisory personnel of each agency. For classified state employees, salary levels are determined by supervisory personnel within each agency based on the salary range for an employee's assigned pay grade as established by Human Resource Management Services, and total salaries for the biennium must be within the agency's salaries and wages line item appropriation approved by the Legislative Assembly. Unclassified employees' salary levels are determined by the governing body or supervisory personnel of the agency and total salaries for the biennium must be within the agency's salaries and wages line item appropriation approved by the Legislative Assembly.

Fringe benefits for state employees include:

1. Social Security/Medicare benefits - 7.65 percent of salary provided by the employee and 7.65 percent of salary provided by the state.
2. Retirement benefits - Percentage varies by type of employee.
3. Single or family health insurance policy paid for by the state.
4. Term life insurance policy with a value of $1,300 at a cost of 28 cents per month per employee.
5. Employee assistance program paid for by the state at a cost of $1.42 per month per employee. This program provides guidance and counseling or a determination of the appropriate diagnosis or course of treatment for employees and their eligible dependents in cases of alcoholism, drug abuse, or other personal problems.
6. Annual leave, sick leave, family leave, funeral leave, and holiday leave.
7. Workers' compensation.
8. Unemployment insurance.

Salary Increase History

The committee reviewed the following summary of state employee salary increases and the cost of providing salary increases for the 1997-99 through 2005-07 bienniums:

STATE EMPLOYEE SALARY INCREASES				
Biennium	**Percentage Increase**	**General Fund**	**Special Funds**	**Total**
1997-99	3% on July 1, 1997 (includes 1.5% for merit) and 3% on July 1, 1998 (includes 1.5% for merit)	$24,304,117	$12,520,861	$36,824,978
1999-2001	2% with a $35 per month minimum on July 1, 1999, and 2% with a $35 per month minimum on July 1, 2000	$17,681,836	$9,633,401	$27,315,237
2001-03	3% with a $35 per month minimum on July 1, 2001, and 2% with a $35 per month minimum on July 1, 2002	$27,043,178	$12,493,632	$39,536,810
2003-05	Up to 1% on January 1, 2004, and up to 2% on January 1, 2005 (based on the elimination of positions and savings from vacant positions)			$0
2005-07	4% on July 1, 2005, and 4% on July 1, 2006	$19,778,486	$21,746,666	$41,525,152

For the 2005-07 biennium, a 1 percent state employee salary increase, excluding higher education institutions, costs an estimated $3.6 million per year, of which $1.7 million is from the general fund and $1.9 million is from federal or special funds.

Equity Adjustments

The committee learned in recent bienniums the Legislative Assembly has provided funding, in addition to general across-the-board salary increases, for pay or market equity adjustments for state employees. The funding has been appropriated either to OMB to distribute to classified state employees in various agencies or directly to selected agencies. The schedule below presents the funding appropriated by the Legislative Assembly for these equity increases since the 1999-2001 biennium:

	General Fund	Special Funds	Total
1999-2001 Biennium			
Equity adjustments - Classified employees	$2,700,000	$2,700,000	$5,400,000
University System salary pool	2,685,227		2,685,227
Merit increases - Department of Transportation engineers		800,000	800,000
Equity adjustments - Elected and appointed officials	77,000	22,000	99,000
Equity increases for Information Technology Department programmers and analysts		317,644	317,644
Equity increases for State Auditor's office	38,000		38,000
Public Employees Retirement System		33,574	33,574
Department of Public Instruction information technology staff	72,444		72,444
Agricultural Experiment Station/Extension Service, Transportation Institute, Northern Crops Institute	422,400		422,400
Total 1999-2001	$5,995,071	$3,873,218	$9,868,289
2001-03 Biennium			
Equity adjustments - Classified employees	$2,700,000	$2,300,000	$5,000,000
Pay grade minimum adjustments - Classified employees	360,797	131,505	492,302
Equity adjustments - Elected and appointed officials	142,697	35,536	178,233
Equity adjustments - Supreme Court and district court judges	724,451		724,451
Equity adjustments - Department of Corrections and Rehabilitation	422,528		422,528
Equity adjustments - Department of Transportation		1,200,000	1,200,000
Total 2001-03	$4,350,473	$3,667,041	$8,017,514

	General Fund	Special Funds	Total
2003-05 Biennium			
Equity adjustment - Legislative Council	$150,000		$150,000
Equity adjustment - Public Employees Retirement System		$80,362	80,362
Equity adjustment - Attorney General's office for assistant attorneys general		241,024	241,024
Equity adjustment - Department of Human Services Program and Policy Division		131,784	131,784
Equity adjustment - Department of Financial Institutions		167,000	167,000
Equity adjustment - Department of Corrections and Rehabilitation Juvenile Services Division	99,856		99,856
Total 2003-05	$249,856	$620,170	$870,026
2005-07 Biennium			
Equity adjustment - Department of Corrections and Rehabilitation	$1,500,000		$1,500,000
Equity adjustment - Highway Patrol	166,258	$28,209	194,467
Total 2005-07	$1,666,258	$28,209	$1,694,467

Retirement

The committee learned North Dakota Century Code Chapter 54-52 provides that employees who are 18 years of age or older, whose services are not limited in duration and who are filling an approved and regularly funded position in an eligible governmental unit, and are employed at least 20 hours per week at least 20 weeks each year, are eligible to participate in the state retirement system. The system consists of two plans--the defined benefits plan administered by PERS and the defined contribution plan. Only certain employees are eligible to participate in the defined contribution plan. Pursuant to Chapter 54-52.6, a permanent state employee, except an employee of the judicial branch or an employee of the State Board of Higher Education and state institutions under the jurisdiction of the board, who is in a position not classified by Human Resource Management Services, may elect to participate in the defined contribution retirement plan.

The defined contribution plan allows the participating employee to control the investment of funds in the employee's own retirement account into which the employee and state contributions are deposited. Retirement benefits are dependent upon the employee's account value at retirement.

Under the defined benefits plan, funds contributed are maintained by the employer and the investment of the funds is controlled by the employer. Retirement benefits are specified for participants in the plan. Separate retirement plans are maintained for state employees dependent on the type of position being filled, including the main retirement system, the Highway Patrolmen's retirement system, judges' retirement system, the National Guard law enforcement retirement system, Job Service retirement system, the Teachers' Fund for Retirement, and higher education retirement (TIAA-CREF) systems.

Under the main retirement program, employees are entitled to unreduced monthly pension benefits beginning when the sum of age and years of credited service equal or exceed 85, or at normal retirement age (65), equal to 2 percent of their final average salary for each year of service. The plan permits early retirement at ages 55 to 64, with three or more years of service.

Benefit and contribution provisions to the plans are administered in accordance with NDCC Chapter 54-52. This statute requires that 4 percent of a participant's regular compensation be contributed to the plan by the employee. During the 1983-85 biennium, the state implemented the employer pickup provision of the Internal Revenue Service Code whereby a portion or all of the required employee contributions are made by the employer. The state chose, in lieu of a salary increase during this biennium, to pay the full employee contribution. Employer contributions of 4.12 percent of covered compensation are set by statute. In addition to the 4.12 percent employer contribution, the state contributes 1 percent of each participating employee's gross wage to a prefunded retiree health insurance program.

As of December 2004 there were 9,868 state employees enrolled in the defined benefits retirement plan and 243 employees in the defined contribution retirement plan.

Health Insurance

The committee learned North Dakota Century Code Chapter 54-52.1 provides that group medical insurance and group life insurance are available to any employee who meets the eligibility requirements of being a permanent employee of the state. A permanent employee is one whose services are not limited in duration, who is filling an approved and regularly funded position in a governmental unit, and who is employed at least 17.5 hours per week at least five months each year or for a person first employed after August 1, 2003, who is employed at least 20 hours per week and at least 20 weeks each year.

The 1963 Legislative Assembly enacted NDCC Chapter 52-12 which authorized state agencies, either individually or jointly with other agencies, to enter a group hospitalization and medical care plan and group life insurance plan for each agency's employees. The agencies were required to pay $5 per month for each participating employee's insurance premium. An employee could elect to participate in either a single or family plan. The 1971 Legislative Assembly repealed Chapter 52-12 and enacted Chapter 54-52.1 establishing the uniform group insurance program. The program was placed under the authority of the Retirement Board. The board was required to solicit bids and contract for the provision of insurance benefits coverage with an insurance carrier determined by the board.

From 1971 to 1983, Blue Cross Blue Shield of North Dakota provided and administered the health insurance benefits plan for public employees. In 1983 the Retirement Board was authorized by NDCC Section 54-52.1-04.2 to establish a plan of self-insurance for providing health benefits coverage under an administrative services-only contract or a third-party administrator contract if the board determined during any biennium that a self-insured plan is less costly than the lowest bid submitted by an insurance carrier. The board exercised the option to implement a self-insurance health benefits plan and administered the program in that manner from July 1, 1983, through June 30, 1989.

Rising health care costs in the state were the primary reason for the cashflow difficulties experienced in the health benefits plan. In the 1985-87 biennium, the Legislative Assembly appropriated funds for a 20 percent premium increase, and claims costs increased 42 percent.

Although the board began its administration of the self-insured health benefits plan on July 1, 1983, with reserves of $2,143,880, claim expenditures and other expenses of the program exceeded premium income and other revenue in 1984 and by June 1987 the fund balance, as indicated in audited financial statements of the plan, was a negative $4,759,963 with estimated outstanding claims payable of $4,600,000.

In 1987 the board incorporated various cost-containment components into the health benefits plan which included:

1. Implementation of a program of concurrent review of inpatient hospitalizations designed to eliminate unnecessary treatment or prolonged hospital stays and to allow consideration of less expensive appropriate treatment for long-term medical care.
2. Implementation of a program of mandatory second surgical opinions for certain elective surgeries. (This program did not generate anticipated results and after a one-year trial period was discontinued.)
3. Expansion of contract deductibles to include all inpatient, outpatient, and physician services.
4. Increase in the coinsurance base from the first $2,000 in charges to the first $4,000 in charges.
5. Implementation of a preferred pharmacy program.
6. Establishment of a separate premium rate for retirees, based on retiree claims experience.
7. Introduction of a $25 copayment for each hospital emergency room visit.
8. Adjustment of the Medicare coordination of benefits formula applied to retiree members of the plan.

Due to the introduction of these cost-containment initiatives and the availability to public employees of a number of attractive health maintenance organization plans, approximately 3,350 membership contracts constituting 23 percent of the total contracts of the health benefits plan were lost during the 1987 open enrollment period, resulting in a decrease of approximately $563,000 per month in premium income.

The decision by the Medcenter One HMO, a health maintenance organization that had the largest PERS-eligible enrollment, to discontinue its participation agreement with PERS as of July 1, 1988, and substantial increases in premiums charged by other HMOs, resulted in a substantial number of public employees choosing the PERS health benefits plan during the 1988 open enrollment period.

In January 1989 the Retirement Board voted to end the state-funded health insurance program and buy the coverage from Blue Cross Blue Shield of North Dakota. Officials of PERS predicted the state would end the 1987-89 biennium with a $3.5 million deficit and would need to increase premium rates by 65 percent in 1989-91. The Blue Cross Blue Shield of North Dakota bid of about $35 million to fund state employees' health insurance for the 1989-91 biennium included provisions that the company would absorb about $5 million in unpaid claims when it took over in July 1989.

Senate Bill No. 2026 (1989) appropriated $1.2 million from the fund for unemployment compensation claims to PERS for the state group health program for the period beginning January 1, 1989, and ending June 30, 1991.

Until 1993 the health insurance program charged premiums based on each employee's election of a single or family plan. Beginning in the 1993-95 biennium, the board began to charge a combination rate that is a blended rate per employee whether a single or family plan is chosen. The blended rate enables agencies to budget the same premium rate for all employees, therefore an agency's budget is not adversely affected if an employee electing to receive single health insurance coverage quits and is replaced by an employee electing to receive family coverage. The schedule below shows the premiums charged since the program began in 1963:

Biennium	Single Plan	Percentage Change	Family Plan	Percentage Change	Combination Rate	Percentage Change
1963-65	$5.00		$21.00			
1965-67	$8.55	71.0%	$21.50	7.1%		
1967-69	$10.75	25.7%	$25.00	16.3%		
1969-71	$14.45	34.4%	$34.90	39.6%		
1971-73	$15.95	10.4%	$41.90	20.1%		
1973-75	$14.46	(9.3%)	$41.90	0.0%		
1975-77	$19.50	34.9%	$59.95	43.1%		
1977-79	$25.50	30.8%	$67.42	12.5%		
1979-81	$34.84	36.6%	$87.40	29.6%		
1981-83	$42.68	22.5%	$107.07	22.5%		
1983-85	$50.28	17.8%	$140.28	31.0%		
1985-87	$60.00	19.3%	$168.00	19.8%		

Biennium	Single Plan	Percentage Change	Family Plan	Percentage Change	Combination Rate	Percentage Change
1987-89	$68.28	13.8%	$191.28	13.9%		
1989-91	$99.82	46.2%	$280.39	46.6%		
1991-93	$108.00	8.2%	$304.00	8.4%		
1993-95					$254.00	
1995-97					$265.00	4.3%
1997-99					$301.00	13.6%
1999-2001					$349.72	16.2%
2001-03					$409.09	17.0%
2003-05					$488.70	19.5%
2005-07					$553.95	13.4%

From 1963 through 1969, the state contributed $5 per month toward the cost of health insurance for state employees. State employees paid any additional amount for single or family coverage. During the 1969-71 biennium, the state contributed $7.50 per month. For the period 1973 through 1979, the state paid the cost of a single health insurance plan. Employees choosing a family plan paid any additional cost. Since 1979 the state has paid the full cost of either a single or family plan for eligible state employees.

The schedule below provides information on health insurance premiums and the cost of health insurance increases since the 1997-99 biennium.

STATE EMPLOYEE HEALTH INSURANCE INCREASES						
Biennium	Monthly Premium	Increase From Previous Biennium	Percentage Increase	General Fund	Special Funds	Total
1997-99	$301	$36	13.6%	$7,026,674	$3,619,802	$10,646,476
1999-2001	$350	$49	16.2%	$6,989,537	$3,858,174	$10,847,711
2001-03	$409	$59	17.0%	$11,182,551	$6,001,252	$17,183,803
2003-05	$489	$80	19.5%	$8,027,122	$8,258,216	$16,285,338
2005-07	$554	$65	13.4%	$5,335,798	$7,903,870	$13,239,668

Holiday Leave

The committee reviewed the following list of statutory holidays cited in NDCC Sections 1-03-01 through 1-03-02.1 on which North Dakota state offices are closed:

- Every Sunday.
- January 1 - New Year's Day.
- The third Monday of January - Martin Luther King Day.
- The third Monday of February - Recognition of the birthday of George Washington.
- The Friday preceding Easter Sunday - Good Friday.
- The last Monday of May - Memorial Day.
- July 4 - Independence Day.
- The first Monday of September - Labor Day.
- November 11 - Veterans Day.
- The fourth Thursday of November - Thanksgiving Day.
- December 25 - Christmas Day.
- Every day appointed by the President of the United States or by the Governor of this state for a public holiday.

If a holiday falls on Saturday or Sunday, the preceding Friday or following Monday, respectively, is considered the holiday. Also, state offices close at noon on December 24, but this is an office closure, not a holiday. The noon closure applies only on December 24 and is not moved to the preceding Friday or following Monday.

Annual Leave and Sick Leave

The committee learned that, according to NDCC Section 54-06-14, annual leave and sick leave must be provided for all permanent employees of the state who are not employed under a written contract of hire setting forth the terms and conditions of employment.

According to North Dakota Administrative Code Chapter 4-07-12, all state and local government agencies, departments, institutions, and boards and commissions that employ individuals in positions classified by Human Resource Management Services are recommended to use the following annual leave schedule:

Years of Service	Hours Per Month	Hours Per Year
0-3	8	96
4-7	10	120
8-12	12	144
13-18	14	168
Over 18	16	192

According to North Dakota Administrative Code Chapter 4-07-13, all state and local government agencies, departments, institutions, and boards and commissions that employ individuals in positions classified by Human Resource Management Services are recommended to use the sick leave accumulation rate of eight hours per month.

Employees who are eligible for annual and sick leave begin to accrue leave from the day of hire. The accrual of annual leave is limited in that no more than 240 hours of annual leave may be carried forward from one year to the next, according to the cutoff date established by the agency. Any hours in excess of 240 will be lost. All accrued, unused sick leave may be carried over from one year to the next, and NDCC Section 54-06-14 provides for a lump sum payment equal to one-tenth of the pay attributed to an employee's unused sick leave accrued to an employee with at least 10 continuous years of state employment.

Under NDCC Sections 54-06-14.1 and 54-06-14.2, a state employee may, under certain instances, donate either annual leave or sick leave to another state employee who is suffering or has a relative or household member suffering from an illness, injury, impairment, or similar condition.

Family Leave - Family Sick Leave

The committee learned North Dakota Century Code Chapter 54-52.4 provides for family leave that is an unpaid leave of absence available to an employee for the birth, adoption, or foster placement of a child; or for the serious health condition of a parent, child, spouse, or employee to all state employees who have been employed by the employer for at least 12 months and who has worked at least 1,250 hours for the employer over the previous 12 months.

North Dakota Century Code Chapter 54-52.4 also provides that an employer who offers compensated leave to its employees for illnesses or other medical or health reasons should allow an employee to use that leave as family sick leave when there is an illness or medical need in the employee's family. Employees are limited to using 40 hours of sick leave for this purpose in any 12-month period.

Findings

Employee Class Evaluation System

The committee reviewed information on the Human Resource Management Services class evaluation system and learned it provides a structured and consistent method of evaluating jobs. Human Resource Management Services, as part of its system, quantifies the factors used for valuing a job in the classification system. The factors evaluated include the knowledge and skills required for the job, the complexity, the accountability of the position, and the working condition hazards. The division then conducts market surveys to determine the appropriate pay for a particular job. These surveys are periodically updated. Prior to the 2003-05 biennium, North Dakota updated its midpoint salaries biennially to 95 percent of the previous year's market level. No changes were made in the 2003-05 biennium, and in the 2005-07 biennium, the midpoints were adjusted by 4 percent each year. In 2006, the majority of salary midpoints range from 83 to 89 percent of market. Market comparisons are made to Job Service North Dakota labor market information for grades 1 through 10 and to a 10-state market sample including the states of Colorado, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, Oklahoma, South Dakota, and Wyoming for grades 11 through 20. Pay ranges are based on the salary range midpoints with the salary range minimum being 25 percent less than the midpoint and the salary range maximum being 25 percent more than the midpoint. Based on 2006 market comparisons, the committee learned North Dakota classified employees' salaries in grades 4 through 15 are lagging the market by 11 to 17 percent, compared to a 12 to 25 percent lag in 2005.

The committee received information on state employees as of August 2006. As of August 2006, state agencies employed 6,384 classified employees with an average employee age of 46.2, average years of service of 13.4, and an average annual salary of $35,640.

Agency Pay Increase Systems

The committee learned some agencies have developed systems for providing salary increases separate from general legislatively authorized increases. Agencies with formalized systems of providing salary increases include the judicial branch, Board for Career and Technical Education, Workforce Safety and Insurance, Highway Patrol, and Adjutant General.

The judicial branch has developed its own salary system consisting of 52 job classifications and 23 salary grades. In addition to the general salary increases authorized by the Legislative Assembly, the judicial branch uses a step system to move employees through their assigned salary ranges. The step increases are provided to employees initially upon the completion of their probationary periods and then every other year thereafter. An employee is eligible to receive a step increase only if the employee's performance is acceptable. Assuming acceptable performance, an employee staying in the same pay grade would move from the pay grade minimum to the maximum after 19 years of employment.

The Department of Career and Technical Education has been using its performance-based salary increase policy since 2003. In addition to the general salary increases provided by the Legislative Assembly, each year, during an employee's employment anniversary month, the employee's performance is evaluated. As a result of the employee's performance evaluation, employees receive "shares" which convert into an additional salary increase. In recent years, each share's value has been $18 per month; therefore, an employee receiving the maximum of three shares would receive an additional salary increase of $54 per month. The performance-based salary increases cost approximately .9 percent of the total salaries appropriation of the department.

Workforce Safety and Insurance was authorized by the 1995 Legislative Assembly to establish its own personnel system. As a result, the agency has developed a pay for performance system that ties the employees' goals to the organization's goals and objectives and establishes clear expectations for employees. The system includes four components:

1. Planning performance - Performance plans are developed for each employee at the beginning of the performance management cycle. Each employee is assigned three to five individual goals that are linked to departmental objectives.
2. Coaching performance - Employees receive advice and assistance to meet or exceed their established performance expectations. The coaching occurs throughout the year and a midyear review is useful for discussing the results to date to identify performance results

that are not adequate and develop plans for improving performance before the final review.

3. Reviewing performance - An employee's actual performance is compared to the established performance expectations through a formal review process. Through the review, managers and employees outline major strengths, areas for development, and action plans to assist in improving performance in certain areas.
4. Rewarding performance - The pay for performance system must be administered consistently throughout the agency. The system rewards employees commensurate with their performance. Employees who perform better receive higher levels of reward and recognition. Recent performance increases provided to employees in addition to the general increases authorized by the Legislative Assembly are 2003 - 3.74 percent, 2004 - 3.06 percent, and 2005 - 3.24 percent.

The Highway Patrol has administered a step system for providing salary increases to its troopers for 30 years. These step increases are in addition to the general increases authorized by the Legislative Assembly and are based on each employee's performance. The system provides step increases through the first 10 years of service. A trooper serving in the trooper's 10th year receives a salary at 45.5 percent of the pay grade. Two additional steps are available. At the beginning of a trooper's 13th year of service, the salary will increase to 50.4 percent of the pay grade and at the start of the 16th year, the trooper's salary will be 55.5 percent of the pay grade. The maximum base pay for a trooper under the current pay structure is attained in the trooper's 16th year. The Highway Patrol believes its salary increase system is very important in its ability to recruit and retain employees.

The Adjutant General has administered a step program for providing salary increases in addition to the legislatively authorized increases since the 1999-2001 biennium. The step increases are based on longevity and satisfactory performance by an employee. The additional cost for providing these increases for the 2005-07 biennium is estimated to total $110,000, of which $45,000 is from the general fund. The additional general fund money needed for these increases is provided from savings resulting from employee turnover.

Health Insurance

The current Public Employees Retirement System health plan with Blue Cross Blue Shield of North Dakota is a modified fully insured plan because PERS determines the plan design; losses are limited to the amount of premiums paid; PERS receives interest on plan holdings; and if expenses are less than premiums, PERS receives 50 percent of the first $3 million of gains and 100 percent of any excess. Any gains realized when claims are lower than premiums are used to reduce health insurance premiums for the subsequent biennium. For the 2005-07 biennium, realized gains reduced premiums by approximately $25 per month per contract.

The committee received information on loss ratios of the PERS health insurance plan compared to other health insurance groups. The committee learned a higher loss ratio is beneficial because it indicates that more of the plan's premium dollars are being spent on claims rather than administrative costs. For the 2003-05 biennium, the PERS health insurance plan experienced a 94.3 percent incurred claim loss ratio. The North Dakota Insurance Department reported the following loss ratios for the calendar year ending December 2004 for Blue Cross Blue Shield of North Dakota:

1. Large group - 91.1 percent.
2. Small group - 84.1 percent.
3. Individual - 88.2 percent.

The committee reviewed high-deductible health plans and health savings accounts and learned the following states have implemented high-deductible health plans or health savings accounts--Arkansas, South Carolina, South Dakota, Colorado, Wyoming, and Florida.

The committee received information on other employer practices regarding health insurance benefits. The committee learned that of the 50 states, six states, including North Dakota, pay 100 percent of employees' health insurance premiums. Compared to the monthly employer contribution for a family health insurance premium which ranges from $704 to $758 among the central states of Colorado, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, Oklahoma, South Dakota, and Wyoming, North Dakota's monthly cost is $554 per single/family contract. The Public Employees Retirement System estimates North Dakota's monthly cost of a family plan to be $643. Based on information provided by Job Service North Dakota, the committee learned that 73.8 percent of employers in North Dakota provide a health plan for full-time salaried employees. The committee learned Basin Electric Power Cooperative conducted a survey in 2004 of 20 major North Dakota employers and found that family health insurance premiums ranged from $450 to $1,043 per month. Of the 20 employers, 7 paid 100 percent of the single premium and 5 paid 100 percent of the family premium.

The committee received information on projected health insurance premium rates under the uniform group insurance program for the 2007-09 biennium. The committee learned the Blue Cross Blue Shield of North Dakota bid for the uniform group insurance program for the 2007-09 biennium for a blended single/family rate is $681 per month, a $127.06 increase or 22.9 percent compared to the current monthly premium rate of $553.94. The rate increase is estimated to cost state agencies an additional $24.4 million for the 2007-09 biennium, of which $11.2 million is from the general fund.

Fringe Benefits Comparison

The committee received the following schedule prepared by Human Resource Management Services comparing the value of fringe benefits of North Dakota state employees to the average employees in the 10 states of Colorado, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, Oklahoma, South Dakota, and Wyoming. The information is based on a state employee with five years of service and an annual salary of $40,035.

Benefit	North Dakota Per Hour Benefit Value	10-State Average Per Hour Benefit Value
Vacation leave	$1.11	$1.14
Sick leave	$.89	$.98
Holiday leave	$.78	$.79
Employer cost share of full family health insurance	$3.75	$4.34
Dental insurance	$0	$.12
Life insurance	Less than 1 cent	$.04
Retirement	$1.76	$1.58
Social Security	$1.19	$1.19
Total benefit value	$9.48	$10.02
Percentage of salary	49.23%	52.04%

Employee Turnover Rates

The committee reviewed information on employee turnover rates of state agencies. The committee learned the total turnover rate for 2005 for all agencies was 9.2 percent, which was the highest turnover rate since 1997; however, North Dakota's rate was less than the 10-state average of 11.3 percent.

The committee received information on significant classified state employee turnover by job type and by agency during the first year of employment. In 2005, of the 123 employees who left state employment during their first year of employment, 57, or 46 percent, were in social services-related jobs; 16, or 13 percent, in medical or health-related jobs; 15, or 12 percent, in miscellaneous administrative positions; and the remaining 35, or 28 percent, in other jobs. The agencies in which most of the employees who left during the first year were located include the Department of Human Services with 60 percent, the Veterans Home with 9 percent, and Job Service North Dakota with 7 percent. The majority of social services-related employees leaving during the first year are lower-paid, direct-care staff at the State Hospital and the Developmental Center.

The following schedule presents turnover rates for major state agencies for recent years:

	Fiscal Year 2004		Fiscal Year 2005		Fiscal Year 2006	
	Total Turnover Rate	Turnover Rate Due to Retirements	Total Turnover Rate	Turnover Rate Due to Retirements	Total Turnover Rate	Turnover Rate Due to Retirements
Bank of North Dakota	7%	2%	6%	2%	9%	1%
Department of Corrections and Rehabilitation	13%	1%	11%	1%	11%	2%
State Department of Health	9.9%	2.5%	12.8%	2.2%	8%	1.3%
Department of Human Services[1]	12.5%	1.9%	13.4%	2.2%	8%	1.8%
Information Technology Department	6.2%	.9%	6.6%	.9%	10.3%	.4%
Job Service North Dakota	9%	3.5%	13%	4.8%	18%	5.4%
Department of Public Instruction	12%	3%	7%	3%	9%	1%
Department of Transportation	5.5%	2.3%	6.5%	2.9%	6.6%	2.4%

[1]Information is provided for calendar years 2004 and 2005 and for the first six months of calendar year 2006.

The committee received information on state agency efforts to recruit and retain employees using nontraditional or nonmonetary benefits. The most common nontraditional or nonmonetary benefits used to recruit and retain employees reported by state agencies include compensatory time, flexible work schedules, tuition assistance, casual days, allowing infants to be brought to work by employees, and recruiting and retention bonuses.

Compensation System Considerations

The committee received information from Human Resource Management Services indicating there are generally two basic pay philosophies--the entitlement philosophy and the performance-oriented philosophy. Under the entitlement philosophy, automatic increases are given to employees each year and the majority of employees receive the same or nearly the same percentage increase. This philosophy is based on the premise that individuals who have worked another year are entitled to a raise in base pay and that incentives and benefits programs should continue and be increased, regardless of changing industry or economic conditions. Under the performance-oriented philosophy, no one is guaranteed a compensation increase each year. Instead, pay and incentives are based on performance differences among employees. Employees who perform well get larger increases and those who do not perform satisfactorily receive little or no increase in compensation.

The committee received information on options for the development of a pay for performance compensation system for state employees. Two models were reviewed. Under the first model, performance increases are provided as a percentage of salary followed by a flat equity dollar increase. Under the second model, a percentage equity increase is provided followed by a flat dollar amount for a performance increase.

The committee received information on the projected cost of increasing salary range midpoints to 90 percent of market, 95 percent of market, and 100 percent of market. The committee learned increasing salary range midpoints to 90 percent of market would require 124 employees to receive salary adjustments to maintain their salaries within the salary range, requiring an estimated $246,000 per year of additional funding. To increase the midpoints of the salary range to 95 percent of market would require 516 employees to receive salary adjustments to maintain their salary levels within the salary range minimum, requiring an estimated $720,000 per year of additional funding. To increase the salary range midpoints to 100 percent of market would require 1,122 employees to receive salary adjustments to maintain their salary levels within the salary range minimum at an estimated cost of $1.9 million per year.

The committee reviewed a bill draft requiring a state employee to contribute $75 per month toward the cost of health insurance premiums but allowing the employee to be reimbursed up to $75 per month for living a healthy lifestyle; providing that the state, for employees hired after June 30, 2007, pay for only the cost of a single health insurance premium less any employee contributions; providing the state contribution toward health insurance premiums for part-time employees be proportional to their full-time equivalent percentage; providing employees eligible to receive health insurance but declining coverage to receive up to $100 per month of additional compensation; and precluding agencies from requesting funding for health insurance premiums as part of their budget requests for employees not enrolled in the health insurance program. The bill was withdrawn from further consideration by the sponsor.

2007-09 Compensation Adjustment Suggestions

The committee received a report of the State Board of Higher Education Committee on Employee Compensation. The committee learned the higher education compensation committee recommended:

1. A total combined salary increase of at least 7.4 percent for faculty and 5.4 percent for staff at higher education institutions for each year of the 2007-09 biennium.
2. The state continue to fund 100 percent of the employee health insurance premiums with no changes to deductibles or copayments.
3. The state increase the retirement plan contribution from 10 to 12.5 percent and the employee contribution from 2 to 2.5 percent for employees with over 15 years of service.

The committee learned the State Board of Higher Education, in considering these recommendations, is recommending a salary increase of 5 percent for each year of the 2007-09 biennium.

The committee received a report from the State Employee Compensation Commission regarding its recommendations for state employee compensation for the 2007-09 biennium. The committee learned the commission is recommending the 2007 Legislative Assembly provide a state employee salary increase of 5 percent on July 1, 2007, and 4 percent on July 1, 2008; funding for an $8 million salary equity pool for classified state employees, $4 million of which is from the general fund and $4 million of special funds; and continuing the full state payment of the single or family health insurance premium with no plan changes. The estimated cost of the State Employee Compensation Commission's recommended increases is $40.2 million from the general fund, $25 million of which relates to the 5 percent and 4 percent salary increases, $4 million for the salary equity increases, and $11.2 million for health insurance premium increases.

Other Reports and Testimony

The committee heard other reports, including a report on agencies with human resource directors, state employee salary increases provided during April through September 2005, other states' age and service requirements for retirement benefits, and information on the North Dakota labor market.

The committee heard comments from state agency representatives and other interested persons regarding state employee compensation issues. Major comments and suggestions made include:

1. Salary increases provided in recent years have only provided for cost-of-living increases.
2. State agencies are experiencing fewer applicants for job openings.
3. It is costly to recruit and train a new employee.
4. State employees have continued to provide a valuable service to the state when state revenues were not keeping pace with state funding needs and salary increase funding was not provided. It is important for the Legislative Assembly, during the 2007 legislative session, when state revenues are adequate and large fund balances exist, to adequately reward state employees.
5. Continue to provide the fully paid health insurance premium for employees with no plan changes.
6. Provide salary increases necessary to be competitive with the market.
7. Once salary levels are competitive with the market, establish a performance component to the compensation system.
8. Address pay equity issues among employees in different agencies.
9. Provide a consistent salary administration strategy from year to year.
10. Adjust salary range midpoints to 95 percent of market.
11. Provide funding necessary to allow employees to advance through their salary range through a merit, step, or other system.
12. Allow agencies flexibility with salary funding and fringe benefits to recruit and retain employees.

RECOMMENDATIONS

The committee made no recommendations regarding its study of state employee compensation.