TESTIMONY OF SCOTT MILLER

Senate Bill 2042 – Actuary-Recommended Employer Contribution Increase

Good Morning, my name is Scott Miller. I am the Executive Director of the North Dakota Public Employees Retirement System, or NDPERS. I appear before you today on behalf of the NDPERS Board in support of Senate Bill 2042. Note that the Employee Benefits Programs Committee gave this bill a favorable recommendation.

This bill was originally drafted to comply with NDCC section 54-52-06(4), which requires the following: "The board shall report to each session of the legislative assembly the contributions necessary, as determined by the actuarial study, to maintain the fund's actuarial soundness." At the time we drafted this bill in early 2020, the statutory contribution rate to the Main PERS Plan was 5.12% below the Actuarially Determined Contribution (ADC) rate. That amount was determined pursuant to the 2019 actuarial valuation.

In early 2020 our actuary performed an actuarial experience study, which statute requires us to have done every five years. As a result of that study, the PERS Board adopted several changes to our actuarial assumptions, including updating our mortality tables and reducing our assumed rate of return from 7.5% to 7.0%. Those changes and certain actuarial losses during the 2019-2020 fiscal year increased our unfunded liabilities, which increased the ADC rate by 0.66%, as reflected in our 2020 actuarial valuation. In order to comply with the statutory requirement, I submit the attached amendment to this bill, which changes the contribution increase to 5.78% to equal the current ADC rate.

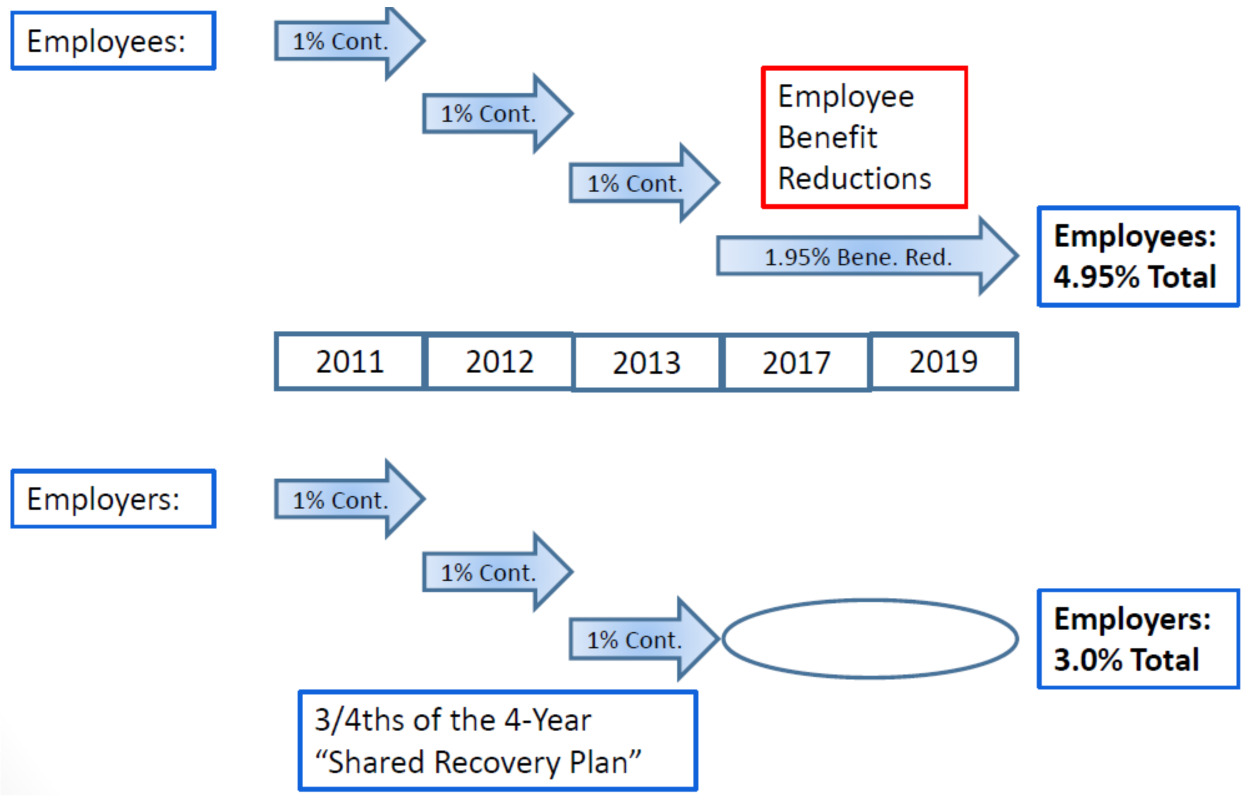
Of course, the reason this bill is necessary is because the main PERS plan is severely underfunded, and is never projected to become fully funded. In fact, we are projected to run out of money in our pension trust within the next 100 years. At that point we will become a pay-as-you-go system, requiring Legislative appropriations every biennium to make hundreds of millions of dollars of retirement payments.

It is not difficult to see how we got to this point. The tech bubble, the Global Financial Crisis, the pandemic; each of them affected our assets negatively. Unfortunately, our contributions have not kept up – we are now nearly six percent below the actuarially determined contribution rate. Because of that, we have experienced actuarial losses every year due to contributions that were lower than the ADC rate – over the past ten years, we have had a contribution deficiency of more than $460 million.

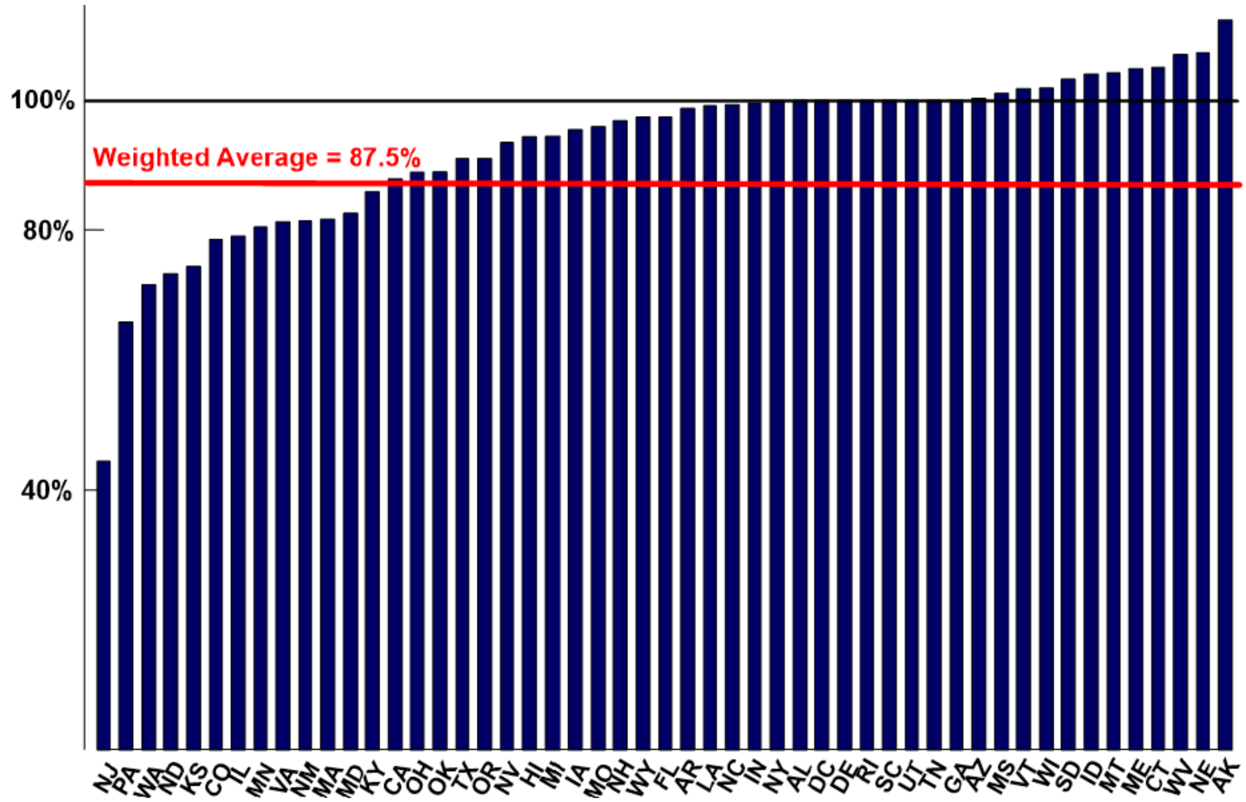
There are very few levers we can use to try to get the PERS plan back on the course to full funding. The general formula for funding a defined benefit retirement plan is below:

Contributions + Investment Returns = ***Benefits*** + Expenses

Since investment returns are not high enough to put us back on the course to full funding, and expenses are not significant enough to have any effect on the equation, we must look at altering either "Contributions" or "Benefits". We have tried pulling both of those levers over the past ten years, implementing both contribution increases and benefit reductions, as you can see below:



This bill, Senate Bill 2042, addresses the "Contributions" side of the equation. Our actuary has calculated that our statutory contribution rate is currently 5.78% below the ADC rate. As a result, we have the fourth-lowest percentage of ADC contributed to the plan in the country, according to the below graph from the National Association of State Retirement Administrators (NASRA). Note that we are below Illinois and Kentucky, two states that are experiencing even more dire funding problems.



Increasing the contribution rate to the ADC will get us fully-funded in the next twenty years, assuming our actuarial assumptions are met. Getting on the course to full-funding is essential for the state's political subdivisions and their GASB liability reporting. GASB stands for "Governmental Accounting Standards Board". GASB provides "statements" that provide guidance for governmental entities, like the state and its political subdivisions, on how to report certain things in their financial statements. In the past few years, GASB issued a statement that requires governmental entities with retirement plans that are not projected to ever reach 100% funding – like the Main PERS plan – to report their liabilities using a discount rate that is below those plans' assumed rates of return. GASB calls that a "single discount rate".

The problem with using that single discount rate is that the rate is significantly below our assumed rate of return – our assumed rate of return is 7.0%, and the single discount rate we had to use last fiscal year is 4.64%. Using a lower rate to determine our liabilities results in a significant increase in those projected liabilities: using the 7.0% rate results in $1.4 billion of unfunded liabilities, whereas using the 4.64% rate results in over $3.1 billion in unfunded liabilities – a 121% increase in the unfunded liabilities.

GASB also now requires the state and its political subdivisions to report that higher unfunded liability figure in their financial statements. As a result, the pension liabilities that have to be reported in the financial statements are 121% higher than they would be if we were on the course to being 100% funded. That is causing a significantly negative impact on many of our participating political subdivisions' financial statements. Those increased liabilities may also result in negative rating outlooks from the rating agencies, or even a reduction in the bond rating for your political subdivisions, increasing their cost of borrowing money. That is one of the reasons it is imperative that we get back on the course to full funding as quickly as possible. It will also help ensure that we do not become like Illinois or Kentucky, both of which are in dire circumstances in part because they did not pay the actuarially determined contribution rate to their retirement plans.

The cost of Senate Bill 2042 is not insignificant. However, keep in mind that without a legislative change, we will become an insolvent, pay-as-you-go system. The question becomes this: do you want to pay for this now, or do you want to pay a lot more for this later? Every day we wait makes it more expensive. The cost now is a small fraction of the hundreds of millions of dollars the Legislature will need to appropriate every year in the future to make ongoing retirement benefit payments.

Thank you for all of your work and support in the past, and for your positive consideration of this Bill.