Testimony in Opposition to House Bill No. 1486

Scott Miller, Executive Director

NORTH DAKOTA
PUBLIC EMPLOYEES
RETIREMENT SYSTEM

$4.5 Billion More Expensive

- This is the present value of how much MORE expensive over the next 22 years it will be to close the Defined Benefit plan and have all new employees go into the new Defined Contribution plan, than it is to maintain the current DB plan
- Unfortunately, you cannot require future Legislatures to maintain adequate funding

Contributions to the DB Plan and DC Plan			
	Present Value of Total Employer Contributions for 2023 to 2045[1]	Difference from Baseline	Difference from Baseline - ADEC Funding
Baseline	$1,628,872,628		
Baseline - ADEC Funding	$2,451,546,855	$822,674,227	
Bill 280 - 6.50% Investment Return	$3,237,625,450	$1,608,752,821	$ 786,078,595
Bill 280 - 5.50% Investment Return	$4,494,009,269	$2,865,136,641	$ 2,042,462,414
Bill 280 - 4.50% Investment Return	$6,165,090,492	$4,536,217,864	$ 3,713,543,637

Credentialed Actuaries

The board shall arrange for actuarial and medical advisers for the system. The board shall cause a qualified, competent actuary to be retained on a consulting basis. The actuary shall make an annual valuation of the liabilities and reserves of the system and a determination of the contributions required by the system to discharge its liabilities and pay the administrative costs under this chapter, and to recommend to the board rates of employer and employee contributions required, based upon the entry age normal cost method, to maintain the system on an actuarial reserve basis; once every

- NDCC section 54-52-04(4), above, requires the NDPERS Board to retain and use a credentialed actuary to do these analyses.
- The Retirement Committee did not have Milliman, its actuary, analyze these bills.
- Any alternative numbers you may have seen are not from a credentialed actuary.
- The NDPERS Board could not rely on anyone other than a credentialed actuary to do these analyses, both from a statutory perspective and a fiduciary responsibility perspective.

Assumed Rate of Return

- The recommendation to use a 4.5% discount rate to value the liabilities and determine the ultimate cost of this proposal came from the NDPERS Board's actuary after significant discussion
- The recommendation is based on several factors:
  - We have about 22 years to accumulate the total amount we will need to pay all future benefits
  - Once the Main PERS Plan is 100% funded, contributions will drop significantly
  - However, at that time we will be paying significant retirement benefits, which will be increasing; those payments will need to be made from the trust, rather than contributions
  - Once we start using trust monies to make payments, we will need to sell illiquid investments – we cannot pay a benefit with a tree, or an office building
  - That will naturally constrain our asset allocation and drive it toward a low risk, fixed income allocation

$457 Million Increase

- The total of additional State and Political Subdivision contributions for the 2023-25 biennium, including the $250 million from the general fund and $70 million from the Legacy Earnings fund
- Next biennium the additional contributions will be $619 million
- State Employer contribution goes up an additional 20.0%, to 28.26% of compensation
- Political Subdivision contribution goes up 20.2%, to 28.46% of compensation
- Agencies with federally-funded positions will need to find alternate funding sources

	2023-2025 Biennium	2025 - 2027 Biennium
State Agencies (20.0% increase)	$ 73,653,046	$ 294,612,286
Counties (20.2% increase)	19,574,972	78,299,888
Cities (20.2% increase)	12,753,642	51,014,568
School Districts (20.2% increase)	26,351,228	105,404,911
Other Political Subs (20.2% increase)	5,037,375	20,149,500
Lump Sum Deposits	320,000,000	70,000,000
Total	$ 457,370,263	$ 619,481,153

Traditional defined contribution plans - disadvantages

- Inefficient use of taxpayer money

- Milliman, the Retirement Committee's own actuarial expert, called Defined Contribution plans an "inefficient use of taxpayer money"
  - Milliman Presentation to Retirement Committee, slide 22 (April 11, 2022).
- Why is it "inefficient"?

- Inefficient use of taxpayer money: need almost twice as much $$s to fund same level of benefits as a DB plan* Still a Better Bang for the Buck: An Update on the Economic Efficiencies of Defined Benefit Pensions, National Institute on Retirement Security, December 2014

- Said another way, you can only get half the benefit in a DC plan for the same cost

Traditional defined benefit plans - advantages

- Efficient use of taxpayer dollars

- The Retirement Committee’s own actuarial expert called Defined Benefit plans an “efficient use of taxpayer dollars”
  - Milliman Presentation to Retirement Committee, slide 16, April 11, 2022
- Employees would receive about twice the retirement benefit in a DB plan for the same cost as a DC plan

$14,700 vs. $3,944-7,640

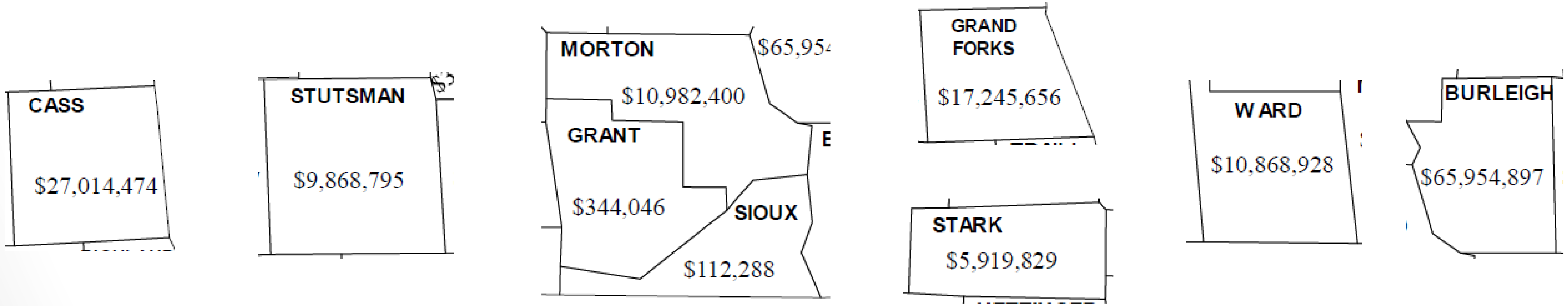
- The average benefit in the DB plan under the Main 2020 Plan versus the average projected benefit under the new DC plan
  - Using average retiree numbers from 2021 valuation (21 years of service, final average salary of $40,000), a 1.75% multiplier, and a DC plan return of 6% compounded annually
  - Depending on the final account balance and whether the individual takes out 3.4% or 4.0% per year
- DC plans are especially difficult for public safety personnel
  - Limited disability and early retirement funds

$200 Million

- NDPERS currently pays out over $200 million in benefits to DB retirees in the State of North Dakota. Every year.
- Total retirement payments to all beneficiaries are over $236 million per year.
- Total employer contributions last year were just under $97 million. Clearly, the return on those contributions is massive.

$100 Million

- Future annual benefits will be cut in half as a result of moving to a DC plan; a DC plan can only provide about half the benefit of a DB plan for the same cost, which will affect all the North Dakota communities you represent
- Similar reduction in economic benefit for your communities



2.87%

- The percent of new employees that elected to join the DC plan from 2013-2017 when it was open and available to all new state employees
- Only 2.36% of 20-somethings elected to join the DC plan at that time
- Current state employees also strongly prefer a DB plan:

Based on the information provided, I prefer to have a defined contribution (DC) retirement plan rather than a defined benefit (DB) retirement plan.* *As stated earlier in this survey a DC plan is similar to the well-known 401(k) and a DB plan is commonly referred to as a pension.	3840	2.18	3%
Based on the information provide, I prefer to have a Defined benefit (DB) Retirement Plan rather than a Defined Contribution (DC) Retirement Plan.* *As defined earlier in this survey a DB is commonly referred to as a pension and a DC is similar to the well-known 401(k).	3858	3.95	42%

Source: 2022 HRMS Survey of Current State Employees

Percent that "Strongly Agree"

Average Rating

75%

- The percent of DC plan members who came back to the DB plan when given the opportunity to do so
- Those members agreed to pay an extra 2% of employee compensation to come back to the DB plan

15.26% vs. 9.26%

- The current DC plan has a mandatory contribution rate for new employees of 15.26%: 7% employee and 8.26% employer
- The new DC plan only has a mandatory contribution rate of 9.26%: 4% employee and 5.26% employer
  - Employee must elect to contribute more, up to 7% employee and 8.26% employer
  - In Oklahoma, only 43% of employees elect to contribute more than the minimum
- Notably, a recent study by the consulting firm Aon and the National Institute on Retirement Security found that a contribution rate of 17% of compensation is necessary for someone to retire at age 67, and 23% to retire at age 62
  - "The Real Deal for the Public Sector: Retirement Income Adequacy Among U.S. Public Sector Employees", Eric Atwater, Tyler Bond, Dan Doonan, Emily Swickard (Dec. 2022).

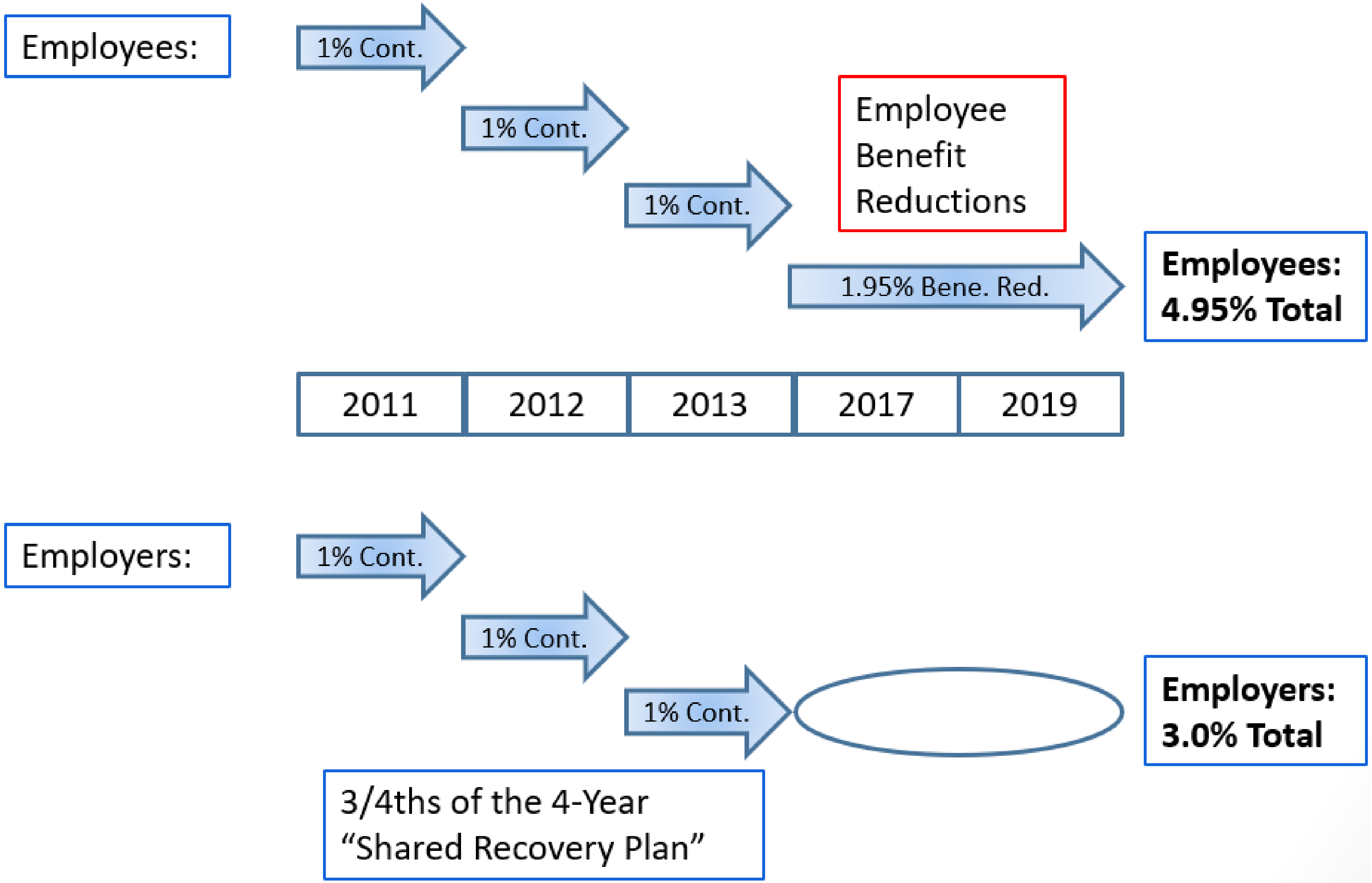
Employees must stay at least 2 years to vest

- The vesting schedule for employer contributions to the DC plan:
  - Under two years of service, 0%
  - Two years of service, 50%
  - Three years of service, 75%
  - Four years of service, 100%
- Always 100% vested in employee contributions

Annuity Default?

- "The qualified default investment alternative must include an in-plan annuity."
- We know of only one qualifying product, from TIAA
  - A complex product participants may not understand
  - Requires the selection of a named fund manager in addition to the underlying investments
  - Moving to a different provider may be difficult, making procurement problematic
  - Likely markedly more expensive than a target date fund
- Note this also places the fiduciary responsibility for setting this default with the Legislative Assembly rather than the Board
  - Investment costs are a primary source of fiduciary litigation
- This requirement basically creates a poor cash balance plan, not a DC plan

Employees Did Their Part



Other States' Experience

- West Virginia – DB closure was far too expensive, and re-opened the DB plan
- Michigan – Closed the DB plan when it was 109% funded, with a $734 million surplus; in September 2019 it was 65% funded with a $6.6 Billion unfunded liability
- Alaska – closed the DB plan in 2005 and has paid billions of dollars more than anticipated; recruitment and retention issues for teachers and public safety have led to significant pressure to re-open the DB plan
- Oklahoma – closed the DB plan in 2018 and created a new DC plan somewhat similar to this bill, and has already had legislative efforts to re-open the DB plan
  - Employer contribution is 16.5% spread over both DB and DC employees
  - Costing the state more than if they had maintained the DB plan
  - Only 43% of new employees elect to contribute above the minimum
  - 87% of members who leave employment take a direct distribution rather than roll-over
  - Recruitment and retention has become a "major issue that is being discussed"

Conclusion:
An Inefficient Decision

- $4.5 billion more expensive over the next 20 years
  - Future Legislatures cannot be required to adequately fund this decision
- DC plans are an "inefficient use of taxpayer money"; DB plans are "efficient"
- DC plans provide half the benefit for the same cost as a DB plan
- Retirement adequacy under the new DC plan is questionable, especially for public safety employees
- The new DC plan may result in significantly lower savings than the existing DC plan
- Employees who leave before completing 2 years of service will not take any of the employer contribution with them
- Neither new employees nor current employees have shown a desire for a DC plan
- The economic benefit to our communities could be halved, if not worse
- Recruitment and retention may become major issues for the state and political subs

Questions?

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