RETIREMENT COMMITTEE

The Retirement Committee was assigned two studies:

- Section 33 of House Bill No. 1040 (2023) directed a study of the Public Employees Retirement System (PERS) main system plan, including funding options and contributions by political subdivisions.
- Section 34 of House Bill No. 1040 directed a study of best practices for public employee retirement plans, including defined benefit (DB), defined contribution (DC), and hybrid plans, such as side-by-side hybrid plans, cash benefit plans, and stacked hybrid plans; and development of legislation to implement the retirement plan best suited to meet the needs of the state, political subdivisions, and public employees.

Committee members were Representatives Jason Dockter (Chairman), Jorin Johnson, Mike Lefor, Scott Louser, SuAnn Olson, Mitch Ostlie, Brandy Pyle, Bernie Satrom, Austen Schauer, and Greg Stemen and Senators Randy A. Burckhard, Dick Dever, Karen K. Krebsbach, Dean Rummel, Shawn Vedaa, and Mark F. Weber.

BACKGROUND

Public Employees Retirement System

Senate Bill No. 154 (1965) created PERS, effective July 1, 1966, as a DC retirement plan. Senate Bill No. 2068 (1977) converted the PERS main system retirement plan to a DB retirement plan. The main system DB retirement plan is funded from employer contributions, employee contributions, and investment earnings. A history of the rates of employer and employee contributions, calculated as a percentage of gross pay, is shown below.

1989 Through December 31, 2011		Effective January 1, 2012		Effective January 1, 2013		Effective January 1, 2014		Effective January 1, 2024	
Employer	Employee	Employer	Employee	Employer	Employee	Employer	Employee	Employer	Employee
4.12%	4.00%[1]	5.12%	5.00%[1]	6.12%	6.00%[1]	7.12%[2]	7.00%[1]	8.12%	7.00%[1]

[1]The state pays 4 percent of the employee share of retirement contributions.

[2]Senate Bill No. 2046 (2019) reallocated the 1.14 percent employer contribution for the retiree health insurance credit to the main system DB retirement plan for employees hired after December 31, 2019, resulting in a total employer contribution rate of 8.26 percent for employees hired after December 31, 2019, and 9.26 percent for employees hired after December 31, 2023.

Benefit Levels and Calculations

Members of the main system DB retirement plan are eligible for a normal service retirement benefit at age 65. Employees hired before January 1, 2016, are eligible for retirement when age plus years of service is equal to 85 (commonly known as the "Rule of 85"). Employees hired after December 31, 2015, are eligible for retirement when age plus years of service is equal to 90 (commonly known as the "Rule of 90") and the member attains a minimum age of 60.

Retirement benefits under the main system DB retirement plan are calculated using the following mathematical formula provided in North Dakota Century Code Section 54-52-17(4):

Final average salary[1] x benefit multiplier[2] x years of service credit[3] = monthly single life retirement benefit

[1]For employees who retired before August 1, 2010, the final average salary was the average of an employee's highest salaries in 36 of the last 120 months worked. For employees who terminated employment after July 31, 2010, but before January 1, 2020, it is the average of the employee's highest salaries in 36 of the last 180 months worked. For employees who terminated employment after December 31, 2019, it is the average of the employee's highest three 12 consecutive month periods of the last 180 months worked.

[2]The benefit multiplier is the rate at which benefits are earned. For main system DB retirement plan members enrolled before January 1, 2020, the benefit multiplier is 2 percent. For members enrolled after December 31, 2019, the benefit multiplier is 1.75 percent.

[3]The service credit is the amount of public service an employee has accumulated under PERS for retirement purposes.

The following schedule is a summary of benefit changes approved by the Legislative Assembly since 1977:

Year	Benefit Multiplier	Change in Retirement Rule Levels
July 1977	1.04%	
July 1983	1.20%	
July 1985	1.30%	Rule of 90 established as an alternative for retirement eligibility
July 1987	1.50%	
July 1989	1.65%	
July 1991	1.69%	
August 1993	1.725%	Rule of 90 changed to Rule of 88
January 1994	1.74%	
August 1997	1.77%	Rule of 88 changed to Rule of 85
August 1999	1.89%	
August 2001	2.00%	
January 2016	2.00%	Rule of 85 changed to Rule of 90 for employees hired after December 31, 2015
January 2020	1.75%	Benefit multiplier of 1.75 percent for members enrolled after December 31, 2019, but remains 2 percent for members enrolled before January 1, 2020
January 2025	1.75%	Closure of the main system DB retirement plan to new hires

Membership

The following schedule is a summary of membership of the main system DB retirement plan as of January 1 of each year:

Calendar Year	Active State Members	Active Political Subdivisions Members	Retirees and Beneficiaries	Deferred Members	Total
2013	10,014	10,264	7,214	7,634	35,126
2014	10,437	11,511	7,907	8,304	38,159
2015	10,536	12,097	8,628	9,503	40,764
2016	10,783	12,750	9,291	10,733	43,557
2017	10,605	12,965	9,790	11,654	45,014
2018	10,237	13,119	10,957	12,186	46,499
2019	10,073	13,343	11,759	13,267	48,442
2020	9,998	13,693	12,117	14,000	49,808
2021	10,553	15,101	13,259	13,887	52,800
2022	10,361	15,253	14,000	15,020	54,634
2023	10,038	14,304	12,910	16,188	53,440
2024	10,090	14,443	13,665	17,074	55,272

Participation of Political Subdivisions

The following schedule shows the number of state agencies and political subdivisions participating in the main system DB retirement plan since 2015:

PERS Retirement Participating Employers[1]

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Counties	49	50	50	50	50	52	52	52	51	51
Cities	85	86	87	87	89	92	90	90	98	100
School districts	119	119	121	121	123	127	128	129	131	133
Other[2]	76	77	78	82	83	81	83	90	93	95
Subdivision subtotal	329	332	336	340	345	352	350	361	373	379
State agencies	94	95	95	95	94	95	96	97	98	100
Total	423	427	431	435	439	447	449	458	471	479

[1]Data presented in this table is as of January of each year.

[2]Other participating political subdivisions include water districts, park districts, and other similar entities.

Assets, Liabilities, and Funded Ratio

The actuarial funded ratio is the percentage of the PERS fund's actuarial value of assets to its actuarial accrued liabilities. The actuarial value of assets is determined by spreading market appreciation or depreciation over 5 years. This procedure results in recognition of the changes in market value over 5 years. The following schedule shows the actuarial assets and liabilities of the main system DB retirement plan since 2000:

Fiscal Year	Actuarial Value of Assets	Actuarial Value of Liabilities	Actuarial Surplus or (Unfunded Liability)	Actuarial Funded Ratio	Assumed Rate of Return[1]	Actuarial Rate of Return[2]	Rate of Return Variance[3]
2000	$1,009,744,796	$879,189,877	$130,554,919	114.8%	8.00%	13.71%	5.71%
2001	$1,096,115,648	$993,851,809	$102,263,839	110.3%	8.00%	9.36%	1.36%
2002	$1,129,697,099	$1,087,003,336	$42,693,763	103.9%	8.00%	3.91%	(4.09%)
2003	$1,145,284,302	$1,170,477,887	($25,193,585)	97.8%	8.00%	2.18%	(5.82%)
2004	$1,172,258,036	$1,250,849,240	($78,591,204)	93.7%	8.00%	3.16%	(4.84%)
2005	$1,210,287,848	$1,333,491,341	($123,203,493)	90.8%	8.00%	4.36%	(3.64%)
2006	$1,286,478,642	$1,450,113,412	($163,634,770)	88.7%	8.00%	7.79%	(0.21%)
2007	$1,470,367,098	$1,575,666,628	($105,299,530)	93.3%	8.00%	15.84%	7.84%
2008	$1,571,159,912	$1,700,171,588	($129,011,676)	92.4%	8.00%	8.51%	0.51%
2009	$1,577,552,012	$1,861,032,305	($283,480,293)	84.8%	8.00%	1.72%	(6.28%)
2010	$1,576,794,397	$2,156,560,553	($579,766,156)	73.1%	8.00%	1.48%	(6.52%)
2011	$1,603,718,656	$2,284,199,019	($680,480,363)	70.2%	8.00%	3.31%	(4.69%)
2012	$1,579,933,179	$2,442,299,210	($862,366,031)	64.7%	8.00%	(0.15%)	(8.15%)
2013	$1,632,915,720	$2,650,525,018	($1,017,609,298)	61.6%	8.00%	3.93%	(4.07%)
2014	$1,837,902,845	$2,866,511,290	($1,028,608,445)	64.1%	8.00%	12.20%	4.20%
2015	$2,027,476,214	$2,976,071,808	($948,595,594)	68.1%	8.00%	10.01%	2.01%
2016	$2,180,748,616	$3,299,381,100	($1,118,632,484)	66.1%	8.00%	6.59%	(1.41%)
2017	$2,529,631,008	$3,618,083,973	($1,088,452,965)	69.9%	8.00%	8.98%	0.98%
2018	$2,752,053,305	$3,841,701,179	($1,089,647,874)	71.6%	7.75%	9.22%	1.47%
2019	$2,949,967,049	$4,136,252,987	($1,186,285,938)	71.3%	7.50%	8.64%	1.14%
2020	$3,112,920,033	$4,557,679,020	($1,444,758,987)	68.3%	7.00%	7.26%	0.26%
2021	$3,369,943,759	$4,795,054,158	($1,425,110,399)	70.3%	7.00%	10.38%	3.38%
2022	$3,553,539,588	$5,304,187,804	($1,750,648,216)	67.0%	6.50%	7.43%	0.93%
2023	$3,683,545,963	$5,559,270,755	($1,875,724,792)	66.3%	6.50%	6.00%	(0.50%)

[1]Section 2 of House Bill No. 1547 (2023) provides during the 2023-25 biennium, the PERS Board may not reduce the actuarial rate of return assumption for the main system DB retirement plan below 6.5 percent.

[2]The average actuarial rate of return during fiscal years 2000 through 2023 was 6.91 percent.

[3]The average actuarial rate of return during fiscal years 2000 through 2023 was 0.85 percent below the average assumed rate of return.

Defined Benefit Retirement Plan Closure and Contribution Rate Increases

House Bill No. 1040 closes the main system DB retirement plan to new hires effective January 1, 2025. The bill increased the employer contribution rate by 1 percent effective January 1, 2024, resulting in total state and political subdivision employer contributions of 8.12 percent for employees hired before January 1, 2020, and 9.26 percent for employees hired after December 31, 2019, which includes the 1.14 percent that was reallocated from the retiree health insurance credit beginning in the 2019-21 biennium. The employer contribution rate for state agencies will increase again to the actuarially determined employer contribution (ADEC) rate beginning January 1, 2026, to begin paying the unfunded liability of the plan over a closed period of 31.5 years. The employer contribution rate for political subdivisions will remain at 8.12 percent.

Section 3 of House Bill No. 1547 (2023) required PERS to conduct an informational campaign during the 2023-25 biennium to educate current and prospective state employees of the transition from the main system DB retirement plan to the new DC retirement plan.

Defined Contribution Retirement Plan

House Bill No. 1040 provides employees who are hired after December 31, 2024, will be enrolled in the new DC retirement plan. The default employee contribution rate under the new DC retirement plan is 4 percent, but employees may elect to contribute an additional 3 percent. Employers are required to match the employee contribution up to 7 percent. If a state employee in the new DC retirement plan contributes less than 7 percent but participates in the PERS deferred compensation plan, the state employer is required to match contributions from the deferred compensation plan up to a total of 7 percent. The deferred compensation plan option is not available for political subdivision employees. For employees participating in the existing DC retirement plan before January 1, 2025, the employee contribution rate remains at 7 percent and the employer contribution rate remains at 7.12 percent.

The new DC retirement plan has an investment option that must include one or more annuity products as part of the investment menu. The existing DC retirement plan has an investment menu but does not provide for annuity products.

Section 17 of House Bill No. 1040 provided state employees with less than 5 years of experience, who are enrolled in the main system DB retirement plan, the option to transfer to the new DC retirement plan between January 1, 2025, and March 31, 2025. Employees who opt to transfer are eligible for an additional $3,333 state annual contribution each January in 2026, 2027, and 2028.

Contingent Effective Date

Sections 1 through 27 and 29 of House Bill No. 1548 (2023) provide the main system DB retirement plan must close to new hires on a date before January 1, 2025. Section 29 of House Bill No. 1548 provides these sections are effective only if the PERS Board certifies to the Legislative Council on the day before the date identified by the board that PERS is prepared to close the main system DB retirement plan and open the new DC retirement plan.

Funding

Section 31 of House Bill No. 1040 amended Section 57-51.1-07.5 to provide $65 million of the state share of oil and gas tax revenues will be deposited in the PERS fund for the main system DB retirement plan beginning in the 2023-25 biennium. Section 35 of the bill provided for a $135 million transfer from the strategic investment and improvements fund to the PERS fund for the purpose of reducing the unfunded liability of the main system DB retirement plan during the 2023-25 biennium.

During the 2023 legislative session, PERS estimated the cost-to-continue reducing the unfunded liability based on the estimated ADEC rate of 30.5 percent during the 2025-27 biennium was approximately $402 million, of which $154 million was from the general fund and $248 million was from other funds. This total included $65 million of ongoing funding provided from oil and gas tax revenues and other funding necessary for 6 months of the 1 percent employer retirement contribution increase through December 31, 2025, after which the ADEC rate would be applied.

Section 1 of Senate Bill No. 2393 (2023) appropriated $12.5 million, of which $5.5 million was from the general fund and $7 million was from other funds, for an employer retirement contribution pool, related to the increased cost of employer contribution increases for executive branch agencies in House Bill No. 1040, House Bill No. 1183 (2023), and House Bill No. 1309 (2023). Section 17 of Senate Bill No. 2393 identified the additional contributions for each agency. Of the total, $10 million, including $4.2 million from the general fund and $5.8 million from other funds, related to House Bill No. 1040.

Section 1 of House Bill No. 1542 (2023) appropriated $347,518, of which $343,245 was from the general fund and $4,273 was from other funds, to the judicial branch for the cost of the 1 percent employer retirement contribution increase in House Bill No. 1040. Section 4 of House Bill No. 1541 (2023) appropriated $58,283 from the general fund to the Legislative Council for the cost of the 1 percent employer retirement contribution increase in House Bill No. 1040.

Senate Bill No. 2023 (2023) appropriated $372,027 in a newly created DB retirement plan closure line item. Of this amount, $47,027 was for a portion of salaries and wages and related operating expenses for 2 full-time equivalent (FTE) positions that were contingent on the Legislative Assembly closing the main system DB retirement plan, $200,000 was for temporary salaries, and $125,000 was for modification of the PERSLink business system. Of the total, $327,000 was considered one-time funding. In addition, PERS may request the Office of Management and Budget transfer up to $479,660 of additional funding from the new and vacant FTE funding pool to this line item for salaries and wages of the contingent FTE positions.

Public Employees Retirement System Board Membership

Section 1 of House Bill No. 1547 (2023), changed the membership of the PERS Board from 9 members, including 2 members of the Legislative Assembly and 1 member appointed by the Governor, to 11 members, including 4 members of the Legislative Assembly and 4 members appointed by the Governor. The Majority Leader of each house must choose two members to serve on the board. The Governor is required to select one citizen member of the board to serve as chairman. The remaining three members continue to be elected by and from active participating members of PERS retirement plans. The State Health Officer, an individual from the Attorney General's legal staff, and an individual receiving retirement benefits from PERS retirement plans are no longer members. Section 1 of the bill became effective October 25, 2023.

Hybrid Retirement Plans

Cash Benefit Plans

A cash benefit plan is similar to a DB retirement plan but includes hypothetical employee accounts that do not reflect actual contributions or gains and losses. The plan receives yearly contribution credits that can be broken down into a pay credit, typically based on compensation and service, and an interest credit. Similar to a DB retirement plan, the investment risks are borne by the employer. Unlike traditional DB retirement plans, employees have the option to receive their account balance in one lump sum at retirement, or to convert the plan to an annuity.

Side-by-Side Hybrid Plans

A side-by-side hybrid plan combines a DB retirement plan with a DC retirement plan to work in tandem as one plan. The model combines a modest DB retirement plan based upon the employee's final average salary and a separate DC retirement account that run parallel to each other. Side-by-side plans expose employees to greater investment risk than DB retirement plans; however, this type of model can provide better retirement savings for early and mid-career workers due to most DB retirement plan benefits being earned in the final years before retirement. Side-by-side plans require additional administrative needs compared to providing a separate DB retirement plan or DC retirement plan.

Stacked Hybrid Plans

Stacked hybrid plans also combine a DB retirement plan and DC retirement plan, but rather than running parallel as in a side-by-side plan, the DB retirement plan is capped at a certain amount and any additional contributions go into a DC retirement account. Because the annual pension benefit is capped, employees only pay into the DB retirement plan up to the maximum salary amount and once that threshold is met, the DC part of the retirement plan is triggered. This plan structure provides the full benefit of a DC retirement plan to lower earning employees and helps guarantee an average baseline of retirement benefits. Due to the cap on the defined benefit, employees earning more than the threshold will have a lower benefit compared to a traditional DB retirement plan.

TESTIMONY

Public Employees Retirement System

The committee received testimony and periodic reports from representatives of PERS regarding the status of the closure of the main system DB retirement plan and the transition to the new DC retirement plan. The committee also received testimony on the progress of the administrative rulemaking process and the importance of that process aligning with the transition to the new DC retirement plan. Testimony indicated PERS is on schedule to transition to the new DC retirement plan on January 1, 2025.

The committee was informed of the informational campaign efforts undertaken by PERS to educate stakeholders on the impacts of the transition from the DB retirement plan to the new DC retirement plan. Testimony indicated communication efforts associated with the special election window for employees with less than 5 years of service are critical. Other communication efforts included presentations with various political subdivisions, including counties, cities, and schools to ensure a successful transition.

Testimony identified eligibility concerns relating to political subdivision membership in the new DC retirement plan. Under PERS' interpretation of the new statutory language established under House Bill 1040, political subdivisions not already enrolled in the DB retirement plan are unable to enroll in the new DC retirement plan. In addition, political subdivisions participating in the new DC retirement plan on January 1, 2025, are not able to leave the plan. A representative of PERS indicated state employees of entities not subject to budget approval through the legislative process will be offered the incentive to transfer from the DB retirement plan to the new DC retirement plan during the special election window, which may cause budgetary concerns for these entities due to the potential fiscal impact of the incentive and ADEC payments.

Actuarial Reports

The committee received testimony from a representative of Gabriel, Roeder, Smith & Company Holdings, Inc., regarding the unfunded liability of the DB retirement plan. Testimony indicated the main system DB retirement plan unfunded liability as of July 1, 2023, was approximately $1.88 billion and the plan was 66.3 percent funded, compared to an unfunded liability of approximately $1.75 billion and a funded ratio of 67 percent as of July 1, 2022.

The committee was informed of the potential effect of contributing additional funding to the main system DB retirement plan and the impact of closing the plan on a different date and changing the plan's amortization period. Testimony indicated a transfer of $200 million per biennium for 10 bienniums to the main system DB retirement plan would offset the loss of employee contributions on a present value basis and potentially fully fund the plan by approximately 2044 instead of 2056, resulting in cost-savings for the state. Closing the plan on June 30, 2024, would have had an estimated actuarial impact of less than 1 percent of the 30-year total cost. Testimony indicated more active and inactive members are employed by political subdivisions than the state; however, the state has a greater liability because the average pay and years of service of state employees are significantly higher.

Vendor Update

The committee received testimony from a representative of Sagitec Solutions, LLC, regarding PERS system upgrades, programming changes necessary to transition to the new DC retirement plan, the completion date of programming, and ongoing programming needs for the PERS system once the transition is complete.

The committee was informed Empower replaced TIAA as the new recordkeeping vendor for the retirement plans on July 1, 2024. The committee received testimony from a representative of Empower regarding services provided, experience with government DC retirement plans, the conversion strategy from TIAA to Empower, member engagement through education, and administration of the new DC retirement plan.

Political Subdivisions

North Dakota Association of Counties

The committee received testimony from a representative of the North Dakota Association of Counties regarding concerns related to the unfunded liability of the main system DB retirement plan and the responsibility counties will incur as a result. Testimony indicated concerns related to local control and whether counties are permitted to select a plan from the marketplace instead of the new DC retirement plan. Counties expressed concern with the inability of political subdivisions not previously enrolled in the main system DB retirement plan to join the new DC retirement plan.

North Dakota League of Cities

The committee received testimony from a representative of the North Dakota League of Cities regarding the cost of the 1 percent employer contribution increase and challenges cities may encounter while incorporating changes related to the new DC retirement plan. Testimony indicated the main challenges faced by cities relate to staffing and budgetary constraints. Testimony also echoed county concerns related to local control, the ability for cities to seek plans outside of PERS, and the ability for new political subdivisions to join the new DC retirement plan.

North Dakota School Boards Association

The committee received testimony from a representative of the North Dakota School Boards Association regarding potential challenges schools may encounter while incorporating changes related to the transition to the new DC retirement plan, including information technology and timing concerns. Testimony indicated 109 of 168 operational school districts, and 22 separate public education entities, participate in the DB retirement plan and training provided by PERS will be critical to successfully transitioning to the new DC retirement plan.

Interested Organizations

National Conference of State Legislatures

The committee received testimony from a representative of the National Conference of State Legislatures regarding other states that have closed their primary DB retirement plans, including the status of plans in those states and any shortcomings associated with alternative plan designs. Testimony contended the transition from a DB retirement plan to a DC retirement plan has a negative effect on recruitment and retention. According to the testimony, defined contribution retirement plans have better cost predictability, but DB retirement plans are more cost-effective due to longevity risk pooling, lower expenses, and a greater ability to maintain a diverse portfolio.

National Association of Government Defined Contribution Administrators

The committee received testimony from a representative of the National Association of Government Defined Contribution Administrators regarding states that have established a primary DC retirement plan and the status of the retirement plan, best practices for state government DC retirement plans, and benefits and shortcomings of alternative retirement plan designs, including cash benefit plans, side-by-side hybrid plans, and stacked hybrid plans. Testimony indicated the process to transition from a DB retirement plan to a DC retirement plan has taken at least 2 years in other states. The committee was informed options to improve the new DC retirement plan included:

- Enrolling employees in a 7 percent employee contribution rate with an option to opt-out of up to 3 percent of the contribution, rather than enrolling employees in a 4 percent rate with an option to contribute up to an additional 3 percent;
- Eliminating the requirement to provide in-plan lifetime annuities in the plan;
- Allowing employees participating in the plan to be 100 percent vested immediately, rather than having a 2- to 4-year vesting schedule; and
- Considering new ideas discussed in other states for modifying a DC retirement plan, including integrating student loan matching, emergency savings options, and financial wellness into the plan.

Public Finance Authority

The committee received testimony from a representative of the Public Finance Authority and a representative of PFM Financial Advisors, LLC, regarding bonding rates, market conditions, and funding options as a potential avenue for addressing the unfunded liability of the DB retirement plan. The committee was informed of the types of bonds issued by North Dakota, the benefits of tax-exempt and taxable bonds, and the potential risk and budget savings if pension obligation bonding is used to address the unfunded liability of the DB retirement plan. Testimony indicated pension obligation bonds may create budgetary cash flow savings by reducing the unfunded liability associated with a plan and replacing the unfunded actuarially accrued liability amortization payments with lower levels of debt service; however, pension obligation bonds carry risks, including failing to achieve the target investment rate that would create cost-savings.

Office of Management and Budget

The committee received testimony from a representative of the Human Resource Management Services Division of the Office of Management and Budget regarding the status of employee compensation, state employee needs for recruitment and retention, and the future of the main system DB retirement plan. The testimony contended a high-quality retirement plan with a steady employer contribution match is essential to recruitment and retention, and ongoing education and communication with employees will be critical during the transition to the new DC retirement plan.

COMMITTEE CONSIDERATIONS

The committee considered the information provided regarding the closure of the main system DB retirement plan and associated implications of House Bill No. 1040. The committee recognized the implementation of the new DC retirement plan will be ready for the transition on January 1, 2025; however, concerns exist relating to political subdivision eligibility and participation in the new plan.

CONCLUSION

The committee makes no recommendation related to the study of the PERS main system retirement plan.