NORTH DAKOTA LEGISLATIVE MANAGEMENT

Minutes of the

EMPLOYEE BENEFITS PROGRAMS COMMITTEE

Tuesday, October 30, 2012
Harvest Room, State Capitol
Bismarck, North Dakota

Senator Dick Dever, Chairman, called the meeting to order at 9:00 a.m.

Members present: Senators Dick Dever, Ray Holmberg, Karen K. Krebsbach, Carolyn C. Nelson, Ronald Sorvaag; Representatives Randy Boehning, Roger Brabandt, Bette Grande, Ron Guggisberg, Scott Louser, Ralph Metcalf, John D. Wall

Member absent: Senator Ralph L. Kilzer

Others present: See Appendix A

It was moved by Senator Holmberg, seconded by Representative Grande, and carried on a voice vote that the minutes of the September 25, 2012, meeting be approved as distributed.

TEACHERS' FUND FOR RETIREMENT

Chairman Dever recognized Ms. Kim Nicholl, FSA, MAAA, FCA, EA, Senior Vice President and National Public Sector Retirement Practice Leader, The Segal Company, Chicago, Illinois. Ms. Nicholl presented the July 1, 2012, actuarial valuation of the Teachers' Fund for Retirement. A PowerPoint used in her presentation is attached as Appendix B, and a copy of the valuation is on file in the Legislative Council office. She said the purposes of the actuarial valuation are to report the fund's assets, estimate the fund's liabilities, determine the annual required contribution for fiscal year 2013, provide information for annual financial statements, and identify emerging trends. She said in the performance of an actuarial valuation, actuaries gather data as of the valuation date; project a benefit for each member, for each possible benefit; apply assumptions; apply assumptions to benefits to determine a total liability and assign liabilities to service; and apply the funding policy to determine the annual required contribution. Over the life of a pension system, she said, benefits plus expenses must equal contributions plus investment return, and contributions must equal benefits plus expenses minus investment return. She said there are two types of actuarial assumptions--demographic and economic, and actuaries make assumptions as to when and why a member will leave active service and estimate the amount and duration of the pension benefits paid.

Ms. Nicholl said economic assumptions include interest rate, salary increase rates, and payroll growth. She said actuarial consulting firms generally use three actuarial methods--the asset valuation method, cost method, or amortization method.

Concerning the valuation, Ms. Nicholl said the valuation reflects increases in contribution rates, 4 percent for both members and employers. She said the member rate increased from 7.75 percent in fiscal year 2012 to 9.75 percent for fiscal year 2013 and fiscal year 2014 and increases to 11.75 percent for fiscal year 2015 and thereafter. She said the employer rate increased from 8.75 percent in fiscal year 2012 to 10.75 percent for fiscal year 2013 and fiscal year 2014 and increases to 12.75 percent for fiscal year 2015 and thereafter. She noted the increases will revert to 7.75 percent for both members and employers once the funded ratio reaches 90 percent as measured using the actuarial value of assets. She said the market value of assets returned a negative 1.4 percent for the year ending June 30, 2012. She said the gradual recognition of deferred losses resulted in a negative 1.4 percent return on actuarial assets and that unrecognized investment losses represent approximately 6 percent of market assets. She said the net impact on the funded ratio was a decrease from 66.3 percent as of July 1, 2011, to 60.9 percent as of July 1, 2012. The net impact on GASB 25 annual required contribution, she said, was a decrease from 13.16 percent of payroll for fiscal year 2012 to 13.02 percent of payroll for fiscal year 2013. Thus, she said, based on the employer contribution rate for fiscal year 2013 of 10.75 percent, there is a contribution deficiency of 2.27 percent of payroll. She said additional contribution rate increases that become effective on July 1, 2014, will address this deficiency.

Concerning assets, Ms. Nicholl said the market value of assets decreased from $1.726 billion as of June 30, 2011, to $1.654 billion as of June 30, 2012. She said Segal determined the investment return was a negative 1.4 percent, net of investment and administrative expenses. She noted the investment returns calculated by Segal are based on a very simplified approach using annual income and end-of-year data. The investment consultant calculations, she said, are more accurate and are based on daily time-weighted cashflows. The actuarial value of assets, she said, which smooths investment gains and losses over a five-year period, decreased from $1.823 billion as of June 30, 2011, to $1.748 billion as of June 30, 2012. She said the actuarial return was also a negative 1.4 percent, net of investment and administrative expenses. She said the actuarial value of assets is 105.7 percent of the market value of assets, and there is a total of $94 million of deferred investment losses that will be recognized in future years. She said the average annual return on market assets over the past 10 years is 5.5 percent, and the 20-year average is 7.0 percent. She said the average annual return on actuarial assets over the past 10 years is 4.0 percent, and the 20-year average is 6.9 percent.

Ms. Nicholl said the annual required contribution calculated by Segal is 13.02 percent, and the employer contribution rate is 10.75 percent. This results in a contribution deficiency of minus 2.27 percent. However, she said, this is an increase from the negative 4.41 percent deficiency calculated on July 1, 2011.

Concerning the actuarial valuation results, Ms. Nicholl said the actuarial accrued liability increased from $2.750 billion as of June 30, 2011, to $2.872 billion as of June 30, 2012. She said the unfunded actuarial accrued liability increased from $927 million to $1.124 million, and the unfunded actuarial accrued liability is 222 percent of active payroll supplied by the system. She said the funded ratio on an actuarial valuation of assets basis decreased from 66 to 61 percent, and on a market value basis, the funded ratio decreased from 63 to 58 percent. She said the annual required contribution decreased from 13.16 percent of payroll to 13.02 percent of payroll. Compared to the 10.75 percent employer contribution, she said, this results in a contribution shortfall of 2.27 percent. She said the funding period based on the 10.75 percent statutory contribution rate is 51 years but that reflecting the additional 4 percent increase in total contribution rate would result in a funding period of 23 years.

Concerning new GASB requirements and proposed adjustments by Moody's, Ms. Nicholl said GASB 67 replaces GASB 25 and provides for accounting with respect to the retirement plan. She said GASB 67 is effective for fiscal year July 1, 2013, to June 30, 2014. She said GASB 68 replaces GASB 27 and provides for a financial reporting by employers and is effective for fiscal year July 1, 2014, to June 30, 2015. She said the proposals require net pension liability be reported on the employer's balance sheet and in the plan's notes to the financial statements. She said accounting and financial reporting are divorced from contribution requirements, and the annual pension expense for employers is essentially equal to a change in total pension liability during the year, with deferrals of certain items. She said Moody's has issued a request for comment on its proposal to implement four adjustments to pension liabilities and cost information and will use this information to prepare bond ratings.

Employee Benefits Programs Committee Bill No. 99

Ms. Nicholl reviewed Employee Benefits Programs Committee Bill No. 99 [13.0099.03000] and the actuarial analysis (Appendix C) for the bill. She said the bill clarifies that the definition of "actuarial equivalent" is based on actuarial assumptions and methods adopted by the retirement board; adds a definition of "normal retirement age" to the plan by reference to statutory sections describing eligibility rules for unreduced retirement benefits and clarifies that members have a vested right to retirement benefits upon attaining normal retirement age; updates federal compliance provisions of the plan regarding the Internal Revenue Code and the North Dakota Century Code; clarifies that Tier 1 members become vested after earning three years of service and Tier 2 members become vested after earning five years of service, without regard to whether assessments were paid to the fund; and adds a savings clause to the plan provisions whereby the retirement board, with approval of the Employee Benefits Programs Committee, may adopt appropriate terminology as necessary for the plan to comply with applicable federal statutes and rules. She said the bill would have an immaterial actuarial cost impact on the Teachers' Fund for Retirement.

It was moved by Senator Holmberg, seconded by Senator Krebsbach, and carried on a roll call vote that the committee give Employee Benefits Programs Committee Bill No. 99 a favorable recommendation. Senators Dever, Holmberg, Krebsbach, Nelson, and Sorvaag and Representatives Boehning, Brabandt, Grande, Guggisberg, Louser, Metcalf, and Wall voted "aye." No negative votes were cast.

Employee Benefits Programs Committee Bill No. 43

Ms. Nicholl said under current law, the higher contribution rates enacted in 2007 and 2009 are set to revert to 7.75 percent on the July 1 following the first valuation showing that the funded ratio, as measured by the ratio of the actuarial value of assets to the actuarial accrued liability, equals or exceeds 90 percent. Employee Benefits Programs Committee Bill No. 43 [13.0043.02000], she said, increases the trigger-funded ratio for contribution reversion from 90 to 100 percent.

Ms. Nicholl reviewed the actuarial analysis (Appendix D) for the bill. She said the bill would not have an actuarial impact on the fund's liability immediately. However, she said, it would increase the funded status of the plan beginning in 2041 by deferring the contribution reversion to 7.75 percent from 2040 until 2046.

Senator Krebsbach said she is concerned that it may be viewed as a change in commitment if the Legislative Assembly extends the trigger from 90 to 100 percent.

In response to Senator Krebsbach's comments, Representative Grande agreed this is a concern and perhaps the North Dakota School Board's Association and the North Dakota Education Association will address the issue.

It was moved by Representative Grande, seconded by Senator Holmberg, and carried on a roll call vote that the committee give Employee Benefits Programs Committee Bill No. 43 a favorable recommendation. Senators Dever, Holmberg, and Sorvaag and Representatives Boehning, Brabandt, Grande, Louser, and Wall voted "aye." Senators Krebsbach and Nelson and Representatives Guggisberg and Metcalf voted "nay."

Chairman Dever recognized Ms. Fay Kopp, Interim Executive Director, Retirement and Investment Office. Ms. Kopp said the State Investment Board has not made any decisions nor adopted a timeline for the selection of a new executive director and chief investment officer. She said the State Investment Board has named a search committee which is soliciting input from clients of the State Investment Board, and the State Investment Board is also reviewing the structure of the Retirement and Investment Office (RIO).

Chairman Dever recognized Mr. Darren Schulz, Interim Chief Investment Officer, Retirement and Investment Office, who reviewed state investments in the Bakken oil development in western North Dakota. Mr. Schulz said the State Investment Board has adopted a policy of not making explicit investments in the Bakken region because of the state's extensive reliance on oil. He said this is done to manage risk. He said the State Investment Board does not restrict its investment managers from investing in companies active in the Bakken region but does not invest in oil and gas or real estate assets in the Bakken region. In effect, he said, the State Investment Board will not "double down" because the state is already exposed to risk in the oil and gas sector.

Representative Grande said the State Investment Board should adopt a policy of divesting from Iran.

In response to Representative Grande's comment, Mr. Schulz said the State Investment Board does not have an explicit policy prohibiting investment in Iran but will poll its investment managers concerning their Iranian investment policies and report this information to Representative Grande.

In response to a question from Senator Nelson, Mr. Schulz said RIO has adopted a proxy voting policy which it informs its investment managers of so that the managers may vote in accordance with RIO's policy. He said the policy is set by the State Investment Board and conveyed to the investment managers to implement it.

PUBLIC EMPLOYEES RETIREMENT SYSTEM

Chairman Dever recognized Mr. Brad Ramirez, FSA, MAAA, FCA, EA, consulting actuary, The Segal Company, Greenwood Village, Colorado. Mr. Ramirez reviewed the July 1, 2012, actuarial valuations of the Public Employees Retirement System (PERS) main system, judges' retirement fund, National Guard retirement fund, Highway Patrolmen's retirement fund, and the retiree health benefits fund. A copy of the PowerPoint used is attached as (Appendix E), and the actuarial valuation is on file in the Legislative Council office. He said the market value of assets returned a negative .20 percent for the year ending June 30, 2012. He said a gradual recognition of deferred gains resulted in a negative .15 percent return based on the actuarial value of assets. He said unrecognized investment losses represent approximately 6 percent of market assets. He said the funded ratio decreased from 70.5 percent as of July 1, 2011, to 65.1 percent as of July 1, 2012. The market value of combined assets for PERS and the Highway Patrolmen's retirement system, he said, was $1.785 billion versus $1.811 billion a year earlier. The combined actuarial value of assets for PERS and the Highway Patrolmen's retirement system was $1.675 billion compared to $1.700 billion a year earlier. He said the total actuarial value of assets is 93.9 percent of the market value of assets, and unrecognized appreciation or depreciation will be recognized in subsequent valuations. He said the market value of assets decreased from $1.811 billion as of June 30, 2011, to $1.785 billion as of June 30, 2012. He said Segal determined the investment return was negative .20 percent, net of investment expenses. The actuarial value of assets, he said, which smooths investment gains and losses over five years, decreased from $1.700 billion as of June 30, 2011, to $1.675 billion as of June 30, 2012. He said the actuarial investment return was negative .15 percent, net of investment expenses. He said the actuarial value is 93.9 percent of market value, and there is a total of $110 million of deferred investment gains that will be recognized in future years. He said the average annual return on market assets over the past 10 years is 6.4 percent, and the average annual return on actuarial assets over the past 10 years is 4.7 percent.

Chairman Dever recognized Ms. Tammy Dixon, FSA, MAAA, EA, The Segal Company, Greenwood Village, Colorado. Ms. Dixon reviewed the actuarially recommended contributions for PERS retirement plans. For the main system, she said, the contribution deficiency increased from a negative 3.74 percent to a negative 5.62 percent as of July 1, 2012. For the judges' system, she said, the contribution sufficiency decreased from 2.06 percent on July 1, 2011, to .69 percent on July 1, 2012. For the National Guard's system, she said, the contribution deficiency increased from negative .58 percent on July 1, 2011, to a negative .90 percent on July 1, 2012. For the law enforcement with prior main system service plan, she said, the contribution deficiency decreased from a negative 2.65 percent on July 1, 2011, to a negative .85 percent on July 1, 2012. For the law enforcement without prior main system service plan, she said, the contribution sufficiency decreased from .62 percent on July 1, 2011, to .35 percent on July 1, 2012. She said the actuarially recommended contribution for the Highway Patrolmen's retirement system declined from a negative 6.93 percent to a negative 7.63 percent on July 1, 2012.

Concerning the Job Service North Dakota retirement plan, Ms. Dixon said the market value of assets decreased from $85.7 million as of June 30, 2011, to $84.7 million as of June 30, 2012. She said Segal determined the investment return was 3.67 percent, net of investment expenses. The actuarial value of assets, she said, which smooths investment gains and losses over a five-year period, increased from $74.2 million as of June 30, 2011, to $75.1 million as of June 30, 2012. She said the investment return on an actuarial basis was 6.95 percent, net of investment expenses, and the actuarial value of assets is 88.7 percent of the market value of assets. She said there was a total of $9.6 million of deferred investment gains that will be recognized in future years.

Concerning the retiree health insurance credit fund, Ms. Dixon said the market value of assets increased from $58.7 million as of June 30, 2011, to $63.9 million as of June 30, 2012. She said Segal determined the investment return was 2.65 percent, net of investment expenses. The actuarial value of assets, she said, which smooths investment gains and losses over five years, increased from $53.7 million as of June 30, 2011, to $58.3 million as of June 30, 2012. She said the investment return on the actuarial value of assets was 1.83 percent, net of investment expenses, and the actuarial value of assets is 91.2 percent of the market value of assets. She said there is a total of $5.6 million of deferred investment gains that will be recognized in future years. She said the actuarially recommended contribution for the retiree health insurance credit fund decreased from .26 percent on July 1, 2011, to .24 percent on July 1, 2012.

Concerning the valuation results, Ms. Dixon said potential risks to the system include continued aging of population, unforeseen demographic "shocks," and changes in the asset return environment. She said the retirement board should consider projections and studies to help quantify these risks and make changes to the system, if appropriate. She said the asset valuation and amortization methods should be reviewed to make sure they are in line with the retirement board's funding objectives. She said contributions are being made in accordance with the funding policy, but the plans remain unfunded. She noted a change in the policy could accelerate an improvement of the funded ratios.

Mr. Ramirez reviewed several projections which are included in the PowerPoint presentation (Appendix E).

Employee Benefits Programs Committee Bill No. 100

Mr. Ramirez reviewed Employee Benefits Programs Committee Bill No. 100 [13.0100.01000] and the technical comments (Appendix F) for the bill. He said the technical comments prepared for the prior meeting remain unchanged. He said the bill eliminates the level Social Security option as a form of payment for new retirees in the hybrid plan; updates federal compliance provisions of the hybrid plan and Highway Patrolmen's retirement system plan regarding Internal Revenue Code and North Dakota Century Code provisions; establishes a new section in Chapter 54-52.6 for the defined contribution plan regarding federal compliance provisions under the Internal Revenue Code; clarifies the normal retirement date in the hybrid plan for National Guard security officers and firefighters, peace officers, and correctional officers of a political subdivision and peace officers in the Bureau of Criminal Investigation to age 55 and three years of employment in such positions, regardless of whether employment in such positions immediately precedes retirement; for purposes of payment of a member's account balance at death from the defined contribution plan; clarifies rules for beneficiaries; permits the board to use fees collected from service providers to fund administrative expenses of the deferred compensation program; permits the board to pay for third-party vendor administration services of the flexcomp program from revenue generated by that program; and updates the committee name in PERS and the Highway Patrolmen's retirement system statutes. He said the bill would not have a significant actuarial cost impact on the hybrid plan or the Highway Patrolmen's retirement system.

It was moved by Senator Krebsbach, seconded by Representative Grande, and carried on a roll call vote that Employee Benefits Programs Committee Bill No. 100 be given a favorable recommendation. Senators Dever, Holmberg, Krebsbach, Nelson, and Sorvaag and Representatives Boehning, Brabandt, Grande, Guggisberg, Louser, Metcalf, and Wall voted "aye." No negative votes were cast.

Employee Benefits Programs Committee Bill No. 103

Mr. Ramirez reviewed Employee Benefits Programs Committee Bill No. 103 [13.0103.02000] and the technical comments (Appendix G) for the bill. He said the proposed legislation would increase both the employer contribution rates and the member contribution rates that are mandated by statute in the Highway Patrolmen's retirement system, hybrid plan, and defined contribution plan by 1 percent of the member's monthly salary beginning January 2014, plus an additional increase in both employer and member contribution rates of 1 percent of the member's monthly salary beginning January 2015. He said the bill would not have a material actuarial impact on the liabilities of either the hybrid plan or the Highway Patrolmen's retirement system but would positively affect the current funding levels of both systems.

In response to a question from Representative Grande, Mr. Sparb Collins, Executive Director, Public

Employees Retirement System, said the Legislative Assembly could consider including a trigger that the employee and employer contribution increases terminate when the funding level reaches 100 percent.

Chairman Dever recognized Mr. Collins. Mr. Collins presented a schedule (Appendix H) showing the cost in dollars of the proposal and a proposed amendment (Appendix I). He said the proposed amendment would remove the change to Section 54-52-06.4.

It was moved by Senator Holmberg, seconded by Senator Nelson, and carried on a roll call vote that Employee Benefits Programs Committee Bill No. 103, as amended, be given a favorable recommendation. Senators Dever, Holmberg, Krebsbach, Nelson, and Sorvaag and Representatives Guggisberg, Louser, Metcalf, and Wall voted "aye." Representatives Boehning, Brabandt, and Grande voted "nay."

Employee Benefits Programs Committee Bill No. 101

Chairman Dever recognized Mr. Collins who reviewed Employee Benefits Programs Committee Bill No. 101 [13.0101.02000], the review prepared by Deloitte Consulting LLP (Appendix J), and a proposed amendment (Appendix K) for the bill. Mr. Collins said the bill amends the relevant provisions of the North Dakota Century Code to modify the uniform group insurance program's eligibility rules for temporary employees first employed after December 31, 2013, to limit the amount any temporary employee can be required to contribute toward the cost of health insurance coverage. The purpose of the proposed change, he said, is to prevent the state from being subjected to employer-shared responsibility penalties with respect to its temporary employees. The second change, he said, is to ensure the state's high-deductible health plan option can be offered to political subdivision employees and to clarify that political subdivisions are not required to make the same employer contribution to their employees' health savings accounts as the state is required to make to its employees' health savings accounts.

It was moved by Representative Grande, seconded by Representative Boehning, and carried on a roll call vote that Employee Benefits Programs Committee Bill No. 101, as amended, be given no recommendation. Senators Dever, Holmberg, Krebsbach, and Sorvaag and Representatives Boehning, Brabandt, Grande, Louser, and Wall voted "aye." Senator Nelson and Representatives Guggisberg and Metcalf voted "nay."

Employee Benefits Programs Committee Bill No. 102

Chairman Dever recognized Mr. Ramirez. Mr. Ramirez reviewed Employee Benefits Programs Committee Bill No. 102 [13.0102.02000], and the technical comments (Appendix L) for the bill. He said the bill eliminates coverage under the uniform group insurance program for employees who first retire after July 1, 2015, and are not eligible for Medicare upon retirement; expands the permissible types of benefit payments from retiree health insurance credits to include contributions toward hospital and medical benefits and prescription drug coverage under any health insurance program; and expands the permissible types of benefit payments from retiree health insurance credits to include contributions toward dental, vision, and long-term care benefits coverage under the uniform group insurance program. He said Segal estimates the required annual contribution would be approximately $9.0 million, which is approximately 1.09 percent of payroll of all active members in the retiree health insurance credit fund to fund the proposal.

Chairman Dever recognized Mr. Collins. Mr. Collins said the proposal also affects the uniform group health insurance program, and thus the retirement board's health insurance consultant has also reviewed the proposal (Appendix M). He said the consulting actuary estimates that the active premium rates currently charged for the uniform group insurance program will decrease by approximately .9 percent, notwithstanding other medical trend factors as a result of the proposal.

It was moved by Senator Krebsbach, seconded by Senator Nelson, and carried on a roll call vote that Employee Benefits Programs Committee Bill No. 102 be given a favorable recommendation. Senators Dever, Holmberg, Krebsbach, Nelson, and Sorvaag and Representatives Boehning, Brabandt, Grande, Guggisberg, Metcalf, and Wall voted "aye." No negative votes were cast.

UNIFORM GROUP INSURANCE PROGRAM

Chairman Dever recognized Mr. Collins. Mr. Collins presented an update concerning the health plan, pre-Medicare retiree health plan and retiree health credit, retirement issues, and comments on the administrative bill submitted to the committee. A copy of Mr. Collins' PowerPoint presentation is attached as Appendix N.

It was moved by Senator Holmberg, seconded by Representative Boehning, and carried that the Chairman and the staff of the Legislative Council be requested to prepare a report and to present the report to the Legislative Management.

No further business appearing, Chairman Dever adjourned the meeting at 2:30 p.m.

Jeffrey N. Nelson
Committee Counsel

ATTACH:14