[LB486 LB509]

The Committee on Nebraska Retirement Systems met at 12:10 p.m. on Tuesday, February 8, 2011, in Room 1525 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on LB486, and LB509. Senators present: Jeremy Nordquist, Chairperson; LeRoy Louden, Vice Chairperson; Lavon Heidemann; Russ Karpisek; Heath Mello; and Dave Pankonin. Senators absent: None.

SENATOR NORDQUIST: All right if everyone can take their seats, I think we'll go ahead and get started. I'm Jeremy Nordquist. I represent downtown and south Omaha and I serve as the Chair of the committee. Senator Louden, our Vice Chair from the 49th Legislative District, will be opening on his bill. Our committee staff is, to my left is Kate Allen our legal counsel for the committee. To my far right is Trisha Clark, our committee clerk. Our page today is Lisa. And we'll start to my right here with self-introductions.

SENATOR MELLO: Heath Mello, District 5, south Omaha and Bellevue.

SENATOR PANKONIN: Dave Pankonin, District 2, Louisville. (Laugh) Looking for somebody else (inaudible).

SENATOR NORDQUIST: All right. Senator Louden, whenever you're ready, we can get started on LB486.

SENATOR LOUDEN: Thank you, Senator Nordquist and members of the Retirement Committee. My name is LeRoy Louden, that's L-e-R-o-y L-o-u-d-e-n, and I represent District 49. I'm here today to present LB486. LB486 increases the 7 percent annual salary cap to 9 percent and eliminates existing exemptions for purposes of calculating benefits on annual compensation during each of the last five years of employment prior to actual retirement. LB486 also clarifies that contributions must be made on the full amount of compensation received and the Public Employees Retirement Board will not refund contributions made on compensation above the 9 percent salary cap. The new cap and elimination of exemptions would go into effect July 1, 2012. I introduced this bill after reviewing data that was put together by the Nebraska Public Employees Retirement System over the interim. NPERS looked at the number of school retirees over the past five years who have been granted exemptions to the salary cap that are currently allowed under statutes. The two categories that make up the vast majority of the exemptions are from excess compensation that occurs from members who experience a substantial change in employment position, which includes additional job or duty change and excess competition that occurs under collective bargaining agreements. The data reveals a clear trend over the last five years. The percentage of retirees receiving an exemption is going up pretty dramatically each year. In 2006, there was...6.3 percent of the retirees were granted exemptions; and in 2008, it was 32.06 percent of the retirees were granted exemptions; and in 2010, 47 percent of the retirees were granted exemptions. I think we need to do something to address this trend. When a retiree's retirement benefit is calculated on compensation that may be much higher than the amounts of contributions that were paid in by the worker, then an unfunded liability is created. This means other school employee members or the state must pay for these retiree's increase in retirement benefits. I believe increasing the cap from the current 7 percent to 9 percent in exchange for eliminating the exemptions is an equitable solution for all school plan members and for Nebraska taxpayers. There are representatives from the Nebraska Public Employees Retirement System here today who will go into detail about the data and the actuarial review that was conducted by Buck Consultants on this issue. I would be happy to respond to any questions or if any, but I'd prefer you have the technical questions for the technical people. [LB486]

SENATOR NORDQUIST: Thank you, Senator Louden. I'd like to thank you for kind of taking the lead on this and highlighting this issue. I think it's something that needs to be looked at again. I will note that Senator Heidemann, from Elk Creek, and Senator Karpisek, from Wilber, Nebraska, have joined the committee. And then I also neglected to mention to the audience if you have a cell phone, please turn it off. And if you're testifying, please fill out a sheet and submit it to the clerk. Any questions of Senator Louden at this time? Seeing none, thank you. Now we will take proponent testimony. [LB486]

JERRY HOFFMAN: (Exhibit 1) Chairman Nordquist, committee members, my name is Jerry Hoffman, J-e-r-r-y H-o-f-f-m-a-n. I'm here representing the Nebraska State Education Association in support of Senator Louden's bill, LB486. I want to thank Senator Louden for bringing this issue to our attention in early fall of 2010, and began working on it with him at that time, then began to include Phyllis and her fine staff at the state office. Also including Mike Dulaney with the School Administrators Association, want to thank him for his involvement as well. So what you have before you is really a consensus agreement, if you will, on the issue of removing the exemptions and increasing the salary increase in the final 60 months of an employee's career to move that to 9 percent. I want to say that the reason we feel this is so important is the ability to shore up any costs in order to maintain the defined benefit system being solvent for both existing teachers, those who are soon to retire and for the graduates of colleges of education who come out and begin teaching and see the defined benefit retirement system as an incredible benefit for the 30-plus years of their teaching career. So with that, I'd like to...what you have before you is some material...research from Ennis Knupp that was presented in November of 2010 that, as you may have read at that time, identifies the benefits...the economic benefits of a defined benefit system over a defined contribution system in terms of not only the yield or return when markets improve to the beneficiaries of the system, but also offering for the individual a way to invest money that on their own individual basis may not have the wherewithal to manage their portfolio in a way that will yield an income that is secure for them in their retirement years. And it is for that reason that Senator Louden's bill and removing the exemptions helps to maintain solvency of the system. With that, I would conclude my remarks and see if there are any questions that the committee may have of me this afternoon. [LB486]

SENATOR NORDQUIST: Thank you, Mr. Hoffman. Any questions from the committee? Seeing none, thank you. [LB486]

JERRY HOFFMAN: Thank you. [LB486]

SENATOR NORDQUIST: Next proponent testifier. [LB486]

MIKE DULANEY: Senator Nordquist, members of the Retirement Committee, my name is Mike Dulaney, D-u-l-a-n-e-y, and I'm the executive director for the Nebraska Council of School Administrators, also here in support of LB486. I wanted to commend Senator Louden for the way he handled this. We've been meeting with him since before the session and had the opportunity to talk to him about concerns and ideas. And what you have before you in this bill is the culmination of that effort. So we thank you very much. I tell my members all the time and remind them how lucky they are to have a great retirement system as they do. I wish I had that retirement plan. And I remind them of that too. Most people aren't lucky enough to have it. And so I think that this...represents a modest and a reasonable change in the plan to deal with the unfunded liability. We also appreciate working with NSEA and Phyllis and her staff also. I think this was just a great effort all around. And I think Senator Nordquist was also brought into those discussions. And, Kate, thank you very much for your work. With that, we give our support and look forward to working with you on other retirement issues. [LB486]

SENATOR NORDQUIST: Thank you, Mr. Dulaney. Any questions from the committee? Seeing none, thanks. [LB486]

MIKE DULANEY: Thank you. [LB486]

SENATOR NORDQUIST: Any additional proponent testifiers? Seeing none, any opponent testimony? Seeing none, any neutral testimony? [LB486]

PHYLLIS CHAMBERS: (Exhibit 2) Good afternoon, Chairman Nordquist and Retirement Committee members. My name is Phyllis Chambers, P-h-y-l-l-i-s C-h-a-m-b-e-r-s, and I serve as director of the Nebraska Public Employees Retirement Systems. I'm here to testify today in a neutral capacity on LB486. In 2005, LB503 was passed changing the school compensation cap from 10 percent to 7 percent and providing for three exemptions for capping salaries. Those exemptions have previously been mentioned. They were (a) a substantial change in position or duties; (b) the result of a collective bargaining agreement; and (c) the result of a districtwide change. Salaries are capped when members apply for retirement. The salaries are capped on a fiscal year basis for the final 60-month period of employment. The salaries are capped...salaries prior to the five years are not capped. Once the benefit is capped then the retirement is calculated using the three highest 12-month periods prior to the termination date. They may or may not be the same years that were capped. They may or may not be a fiscal year like the capping is done, it's based on the person's last month of employment when that occurs. And they may or may not be consecutive periods. So there's a lot involved and a lot of programming in our calculations for what becomes the retirees final benefit. Since the implementation of the 7 percent salary cap in exemptions in 2006, NPERS has experienced a significant increase in the number of exemptions each of the last five years, as Senator Louden has noted. NPERS queried our data and found that there were 574 retirees last year, out of 1,226 of our retirees in 2010, who had at least one exemption over the salary cap, and that equated to 47.3 percent of the members with exemptions. Now that we have completed five full years of capping and exempting salaries, we have a good idea of the research that approximately 50 percent of our retirees going forward are going to have at least one exemption, unless some changes are made. This pattern has increased our staff workload when calculating retirements. NPERS is required to obtain exemption forms from the school employers, sometimes we make multiple attempts to receive those exemption forms, and sometimes if there's an error we have to go back to the school and get those errors corrected. It has increased our number of days that it takes us to process the benefits and it does cause delays in some of the retirements. Our data shows that the exemptions apply to all salary ranges, not just the higher salaried employees. The annual salary increases over the 7 percent cap range from about $3.47 up to about $56,900. And on average, those people that were above the salary cap averaged about $3,750 in increased salaries, if you extrapolate that over 574 members, that's over $2 million. There are a number of valid reasons for the exemptions. Some employees are changing positions, being promoted and some employees are taking on additional duties. Regardless of the reason, the salary increases exempted by the salary cap are creating an unfunded liability in the plan. This also creates an equity issue when the benefit is being paid for by other members in the school plan or by the state in additional contributions. Our actuary, Dave Slishinsky of Buck Consultants, performed a study using exemption data, comparing 7 percent, 8 percent and 9 percent salary caps. I provided you with a copy of the actuaries study. He looked at NPERS data on the 1,226 school retirees in 2010, and he also looked at 4,926 members who were eligible to retire as of July 1 of last year. Assuming that 50 percent of those in the pool of eligible retirees received an exemption, he determined that the present value of future benefits would be reduced by a little over $1 million if the exemptions were removed and the salary cap was changed from 7 to 9 percent. He also determined that the present value of future benefits would be reduced by $3.8 million if the exemptions were removed and the salary cap was changed from 7 to 8 percent. There is a reduction in our unfunded liability when the exemptions are removed and the salary cap is changed to either 8 or 9 percent. As we examined the budget and funding status of the defined benefit plans the changes to the salary cap and exemptions by LB486 would provide a savings to the school plan. And if you have any questions I'd be glad to answer them. [LB486]

SENATOR NORDQUIST: All right. So thank you for being here, Ms. Chambers. The administrative savings wouldn't be significant, but there would be some time as far as tracking down exemptions, some savings there? It may be hard to quantify and put a fiscal piece on it but it should make the process a little more efficient, is that right? [LB486]

PHYLLIS CHAMBERS: Yes, um-hum. [LB486]

SENATOR NORDQUIST: Okay. Any other questions from the committee? Seeing none, thank you. [LB486]

PHYLLIS CHAMBERS: Okay, thank you. [LB486]

SENATOR NORDQUIST: Any additional neutral testimony? Seeing none, Senator Louden waives closing. That will conclude the hearing on LB486. And Kate Allen, our legal counsel, will open on LB509. [LB486]

KATE ALLEN: Thank you, Chairman Nordquist, members of the committee. My name is Kate Allen, that's K-a-t-e A-l-l-e-n. I'm legal counsel for the committee and I'm here to present LB509 which is introduced on behalf of the Nebraska Public Employees Retirement System. In order to avoid redundancy, I'm going to summarize the proposed changes to the Class V school retirement plan and the duties of the Nebraska Investment Council and a representative from the Nebraska Public Employees Retirement System will summarize the provisions affecting the county, state, school, judges, and State Patrol plans that are administered by NPERS. LB509 deletes the requirement for the Public Employees Retirement Board to provide a comprehensive preretirement planning program to members of the Class V retirement system and adds a new section to the Class V School Employees Retirement Act requiring the Class V board to provide comprehensive preretirement planning programs to their members. Since the Public Employees Retirement Board does not administer or oversee the Class V system, PERB cannot expend any of the other member funds to provide this program to the Class V members. I discussed this provision with Mike Smith, the executive director of the Omaha School Employees Retirement System, and he confirmed that they already provide this program to their members. So this will not create a new obligation for them. LB509 also deletes requirements for the Class V retirement system to file annual plan summaries with PERB and the Nebraska Retirement Systems Committee. Instead the Class V retirement system will be required to annually file its actuarial report with PERB and the committee rather than file this report every four years. Again, in discussions with Mike Smith, the Class V system already conducts an annual actuarial review, so this will not create additional actuarial expenses. And finally, LB509 changes the date from March 15 to March 31 for the Nebraska Investment

Council to provide its annual report to the Retirement Systems Committee. This change is proposed in order to provide the NIC additional time to prepare and publish its annual report. I'd be glad to respond to any questions. [LB509]

SENATOR NORDQUIST: Thank you, Kate. And we can take questions on these portions of the bill, if the committee has any questions. Seeing none, thank you. We'll take NPERS as proponent testimony or neutral. Okay. Is there any proponent testimony on this bill? Seeing none, any opponent testimony? Seeing none, we'll go with neutral testimony. [LB509]

JASON HAYES: Good afternoon, members of the Retirement Committee. My name is Jason Hayes, spelled J-a-s-o-n H-a-y-e-s. I serve as legal counsel of the Nebraska Public Employees Retirement Systems and I'm here today to discuss the technical updates and clarification language for the agency contained within LB509. First, the bill provides for suspension of retirement distributions under the State and County Employees Retirement Acts pending a final outcome of a grievance filed by a member of either plan. The agency has had instances where a terminated employee will take a distribution from their retirement account but later, after a successful grievance hearing, the employee will be reinstated. Under current state law the employee is required to pay back his or her retirement because he or she is treated as having never been terminated in the first place. This leaves reinstated employees in a difficult situation where they are required to pay back such amounts out of their paychecks because often they will have spent all of the money or a significant part of it prior to reinstatement. The change in the bill restricts such distributions until it is determined whether the member will be reinstated by the employer. There have been ongoing discussions with the government employees union regarding this restriction however. NPERS would be agreeable to language that partially restricts rather than fully restricts such a distribution. And the groups are in the process of determining what would be a reasonable limitation so that the member will be able to pay off a distribution in a reasonable amount of time should reinstatement occur. And we certainly appreciate the Chair and the legal counsel with the work on that too. Next, the bill modifies language in the Judges, State Patrol and School Employee Retirement Acts to clarify that members will receive the highest cost-of-living method identified in statute. This is currently how the language is being interpreted and it has been that way for some time, but this clarification will eliminate any ambiguity in statute. The COLA provisions are reorganized under a new section within each act. Previously, those provisions were spread out over four different sections in each plan, so this change will be particularly helpful. The bill also modifies language in the Judges Retirement Act to clarify that an optional form of the benefit may exceed the 70 percent cap once an actuarial factor adjustment is made. Now the judges plan currently is limited by a cap of 70 percent so that the monthly retirement benefit does not exceed the preretirement earnings by more than 70 percent. But once this initial calculation is made, the member may select an annuity which in some instances could result in a slight increase above the 70 percent cap in some months, but actuarially this amount is still equivalent to the other annuity options. Again, this is currently how NPERS is interpreting the language in the section, and this change will help remove any ambiguities that may still exist. Next the bill will allow permanent, part-time county and state employees to participate in their respective plans at age 18 rather than 20. State law currently disallows any part-time employees younger than 20 from participating in the plans. The agency believes that retirement planning and saving should start as early as possible so that a member's plan will be sufficient to meet their retirement needs. This change will give permanent part-time employees 18 and 19 years old the option to contribute if they want. The bill also removes a requirement from the Public Employees Retirement Board to notify the Retirement Committee if local political subdivisions fail to file annual pension plan reports that they currently are required to. These local subdivisions retirement plans are not under the purview of NPERS as it relates to the administration of the defined benefit plans or the state and county plans. LB474, also before this committee, addresses that notification and filing of these reports with the State Auditor's Office. Finally, the bill clarifies that school member employees must make contributions on compensation earned above the current 7 percent salary cap that was just discussed as established in the School Employees Retirement Act. This salary cap applies to the benefit formula calculation found in the plan for determining the three highest years of salary. The salary cap, which currently limits amounts above a 7 percent increase unless exempted in any one year from being used in the formula calculation, but this cap is not intended to change the contribution requirement by employees and employers under the plan. So this deals just with the benefit...the formula, not necessarily the contributions. The agency had a situation a few years ago where a school district unilaterally decreased their contribution amounts collected for salaries received above the salary cap. This change will help delineate the distinction between the contribution requirement and the formula calculation for the benefit. And this concludes my testimony for LB509 and I'm happy to take any questions if you have them. [LB509]

SENATOR NORDQUIST: Thank you, Mr. Hayes. Any questions from the committee? Senator Pankonin. [LB509]

SENATOR PANKONIN: Thank you, Chairman Nordquist. Mr. Hayes, thanks for being here today. And you've been on...when did you start this position? [LB509]

JASON HAYES: With NPERS? [LB509]

SENATOR PANKONIN: Right. [LB509]

JASON HAYES: November 1. [LB509]

SENATOR PANKONIN: November? [LB509]

JASON HAYES: November 1 of 2010. [LB509]

SENATOR PANKONIN: November 1. Obviously, this bill is always the technical changes and cleanup. So there is a process an agency had started before you came with many of these suggestions. And you followed up on them or...this is a process question. How does this work to bring these technical changes? [LB509]

JASON HAYES: Some of them were already set aside to be brought forward. And then I went ahead and worked with the legal counsel of the committee to get those in the bill, others came about over the past few months. [LB509]

SENATOR PANKONIN: Since you've been on board and... [LB509]

JASON HAYES: Since I've been on board, yes. [LB509]

SENATOR PANKONIN: Right. So there's a process in the NPERS system that when things are found and whatever that they're kept on a punch list and that sort of thing? [LB509]

JASON HAYES: Um-hum, always trying to improve, always trying to update with other changes in state law as well as to clarify. Certainly there are things that the Auditor's Office points out to NPERS that we want to help do the best that we can so that our members can read the statute and it's very clear, so they know the retirement benefit that they can count on. [LB509]

SENATOR PANKONIN: Okay, thank you. [LB509]

SENATOR NORDQUIST: Okay. Any additional questions for Mr. Hayes? Seeing none, thank you. [LB509]

JASON HAYES: Thank you. [LB509]

SENATOR NORDQUIST: Any additional neutral testimony? [LB509]

JULIE DAKE ABEL: Good afternoon, Chairman Nordquist and members of the Retirement Committee. My name is Julie Dake Abel, D-a-k-e A-b-e-l, and I'm the executive director of the Nebraska Association of Public Employees, AFSME Local 61. We are here today to testify in a neutral position on LB509 and particularly on the section that talks about if an employee is terminated and has a grievance pending then what would happen to their retirement benefits should they want to draw on that. I won't...I'll try not to duplicate anything that Mr. Hayes said from NPERS. I just would like to go on record to say that we have been working with NPERS and with Chairman Nordquist and Kate. And we believe that we will be able to work out some sort of resolution so employees may be able to draw some money out of their retirement, but it does not put them or the system in a bad place where the system cannot recoup the money or the employees take out such an amount that they are unable to repay that. And I would be happy to answer any questions. [LB509]

SENATOR NORDQUIST: Great. Thank you. Any questions from the committee? Seeing none, thank you. [LB509]

JULIE DAKE ABEL: Thank you. [LB509]

SENATOR NORDQUIST: Any additional neutral testimony? Seeing none, that will conclude the hearing on LB509 and conclude the hearing for the Retirement Committee today. Thank you. [LB509]