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Nebraska Retirement Systems Committee
March 05, 2015

[LB447 LB448]

The Committee on Nebraska Retirement Systems met at 12:00 p.m. on Thursday, March 5, 2015, in Room 1525 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on an actuarial report of the Omaha School Employees' Retirement System, LB447, and LB448. Senators present: Jeremy Nordquist, Chairperson; Al Davis, Vice Chairperson; Mike Groene; Rick Kolowski; Mark Kolterman; and Heath Mello. Senators absent: None.

SENATOR NORDQUIST: We're just about to noon, so I'll say happy noonhour to everybody. If you can take a seat we'll go ahead and get started. We've got a full agenda today and we're going to try to move through this quickly. We really need to be wrapped up by probably 1:20 to accommodate the rest of us having to go to other committees, as well as the committee that uses this room at 1:30 after us. Today we'll have three components to the hearing. First, we'll hear the presentation of the OSERS actuarial evaluation report. Then we will hear LB448 and then LB447. Just a couple notes, please be sure to silence your cell phone. We don't want those to disrupt the recording of the hearing proceedings. If you are going to testify today, in the back corners there are sheets you need to complete to testify. And our page will collect that from you or you can give it to the committee clerk when you come up. For the record, we need everyone to state and spell their name at the beginning of their testimony. Also in the back, there are sheets where you can indicate if you do not want to testify your support or opposition to a piece of legislation. I know somebody asked if we could do a show of hands. That's not typically what we do. The sheets in the back are how you get entered into the record as a supporter or opponent if you don't want to testify. We will take proponent testimony, opponent testimony, and then neutral testimony on the two bills. We will open it up if there is any comment on the actuarial study. To my left is our committee counsel Kate Allen, to my far right, our committee clerk Laurie Vollertsen. And now we will have our committee members starting over here to my right with Senator Groene introduce themselves.

SENATOR GROENE: Senator Mike Groene, Lincoln County, North Platte area.

SENATOR KOLOWSKI: Senator Rick Kolowski, District 31, southwest Omaha.

SENATOR NORDQUIST: I believe Senator Davis, the Vice Chair of the committee, will be joining us shortly.

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

SENATOR KOLTERMAN: Senator Mark Kolterman, District 24, Seward, York, and Polk Counties.

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

SENATOR NORDQUIST: Great. We will go ahead and get started with the actuarial report. We have Pat Beckham from Cavanaugh Macdonald to be here to present today. And the committee members have it in the top of their binder. Welcome.

PATRICE BECKHAM: (Exhibits 1 and 2) Thank you. Just for the record, it's Patrice Beckham, P-a-t-r-i-c-e, Beckham, B-e-c-k-h-a-m. And, yes, I'm with Cavanaugh Macdonald, a consulting actuary to the Omaha School Retirement System. And I believe you all have the presentation that we're going to use this morning to walk through the results. I wanted to spend just a very few minutes on the background of the actuarial evaluation process, what it's intended to do, what's involved, and then jump right in to see what the results of the September 1, 2014 evaluation. OSERS has a September 1 evaluation date. I would prefer to take questions as we go through. So if there's a question just jump in. On slide three, the purpose of the actuarial evaluation is really to annually evaluate the financial health of the system and the direction it's going, just as when we get to a certain age we go the doctor every year to make sure things don't go amiss. That's what we're doing with the retirement system so that changes can be made sooner instead of later if necessary. So we measure something we call liabilities. And those liabilities are future benefit payments. We don't know the exact amount of those because they're dependent on a number of events. So we use assumptions to help us quantify those benefit payments and they are what we call discounted back to today's dollars. And then of course we measure assets. We compare the two and based on the funding policy that the system is using, that determines what we call an actuarial contribution rate. Now the system is funded with a fixed contribution rate. So we use the actuarial contribution rate kind of as a benchmark to evaluate the sufficiency of the current contribution rates rather than the actual amount to go in, in the following year. The actuarial evaluation also provides us with information on the actual experience compared to what the assumptions we're anticipating. And we can measure that for a assumption that we use. So that's an important piece of information. And then we're always kind of putting the valuation results next to each other over a longer span of time to see if there's any trends unfolding of anything that we should be aware of or make the board aware of. On slide four, just a little bit more about the actuarial valuation, it's what we call a snapshot. It just stops everything on September 1: the membership on that date, the asset value on that date. And everything is calculated. If we did the valuation a different day, the results would be different. I mentioned earlier that the future benefit payments are dependent on a number of contingent events. We use actuarial assumptions to help us estimate those. That is intended to be the best estimate, but there clearly are other sets of assumptions that would be considered reasonable or acceptable. If we used a different set of assumptions, we would get different liabilities; and therefore, all the other numbers would change as well. And again, we're using these results to really kind of evaluate the sufficiency of the statutory contribution rates. If you'll look on slide five, a couple of slides on membership because obviously the members is what's driving the liability and the results of the valuation. OSERS had a change in the benefit structure in the 2013

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

Session, and so there is a different benefit structure in place for those hired on or after July 1 of 2013. So you can see in the September 1, 2013 valuation, it was actually a small number of folks already in the new tier. This year there is about 85 percent of certificated members in the original benefit structure and about 15 percent in the new benefit structure and classified members is about the same. On the next slide, slide six, you can see the total membership, kind of big picture. So 7,415 active members, 937 who worked long enough to be vested but are no longer working for the school district, entitled to benefits and...

SENATOR KOLTERMAN: Excuse me.

SENATOR NORDQUIST: Pat, Senator Kolterman would like to ask a question here.

PATRICE BECKHAM: I'm sorry. I'm sorry.

SENATOR NORDQUIST: No, please.

SENATOR KOLTERMAN: That's okay. Could you go back to slide number five.

PATRICE BECKHAM: Be happy to.

SENATOR KOLTERMAN: On tier 2, there's as significant jump from September of '13 to '14.

PATRICE BECKHAM: Right, so...

SENATOR KOLTERMAN: Was that a lot of new hires or was that...?

PATRICE BECKHAM: Well, the new tier was effective July 1, and the September 1, 2013, was the valuation date. So we're only two months of new hires.

SENATOR KOLTERMAN: Okay.

PATRICE BECKHAM: And then from 9-1-13 to 9-1-14 you have 12 months of new hires.

SENATOR KOLTERMAN: But that's...I mean that's a pretty significant.

PATRICE BECKHAM: Right, but your initial measurement was just a very small piece of the year.

SENATOR KOLTERMAN: I understand that.

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

PATRICE BECKHAM: Yeah. But, yeah, it should kind of smooth out a little bit. But as people from tier 1 leave and are replaced with tier 2, that's what going to help bring the cost of the plan down.

SENATOR KOLTERMAN: Yeah, the other one went down. So, okay.

SENATOR NORDQUIST: Senator Groene.

SENATOR GROENE: This is from superintendents down to janitors, right, everybody who is employed by the school?

PATRICE BECKHAM: Yes, sir.

SENATOR GROENE: Even aides, so when you say 12,477, it's everybody.

PATRICE BECKHAM: Yes, it's all school employees. Correct.

SENATOR GROENE: All right.

PATRICE BECKHAM: And the classification back on slide five split that active group into certificated members--teachers, administrators--and classified. That's what that split means. We actually have data reported separately for those groups and we use different actuarial assumptions.

SENATOR GROENE: Which group? Which slide?

PATRICE BECKHAM: On slide five.

SENATOR NORDQUIST: The top is...

PATRICE BECKHAM: The top group is certificated.

SENATOR GROENE: Tier 1 versus tier 2?

PATRICE BECKHAM: No, the grouping, where it says certificated members and classified members.

SENATOR GROENE: Oh, all right. Yep.

PATRICE BECKHAM: That's your breakdown between kind of teachers and nonteachers.

SENATOR GROENE: Sorry.

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

PATRICE BECKHAM: Slide seven, I said we measured the assets. We do not use pure market value in the actuarial valuation due to the volatility in the investment returns. That would create very volatile results when this is a long-term venture and we're looking for kind of more reliable long-term benchmarks. So we use what's called an asset valuation method that kind of smooths out, averages out the highs and the lows in the market. The specific method we use calculates an expected value. So it's takes last year's actuarial value, recognizes money that's coming in, going out, but says what if we earn the benchmark, the assumed return of 8 percent, that's our expected return and then we recognize 25 percent of the difference between actual market value and the expected value. And so it's a market-related valuation.

SENATOR NORDQUIST: Pat, on that real quick, so they're smoothing over four years rather than five I assume.

PATRICE BECKHAM: It's not technically four years because each year...if you just had one year's of experience different than eight, then you had eight every other year, you're only recognizing 25 percent. So the first year it's one-fourth. But then it's one-fourth of three-fourths which is three-sixteenths, which is a little less than 20...you know, it's close but it kind of converges over a longer period of time.

SENATOR NORDQUIST: Okay, okay. Generally, if we're looking at comparing funding statuses of the two plans over the past few years of investment return, having them have a...if you want to call it a shorter smoothing even though that might not be accurate, how...if they were on the same smoothing as us, do you have any sense of would that improve or improve their funding status or make it worse or not make a difference?

PATRICE BECKHAM: Off the top of my head, I'm not sure. They also have a different measurement date...

SENATOR NORDQUIST: Right, okay. Yeah, true.

PATRICE BECKHAM: ...which, you know, you're not really comparing apples to apples. But this method kind of converges back to market a little quicker than the method that the statewide system uses. So it kind of depends on how those numbers are unfolding.

SENATOR NORDQUIST: All right. Thank you.

PATRICE BECKHAM: And on the next slide on eight, again, just gives you a little bit of a historical perspective from 2002-2014, what the return was on market value and actuarial value. And as you'll see, the blue line is market and it's clearly more volatile, more ups and downs. And the red line is the rate of return on the actuarial or the

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

smooth value. We expect to see that line to be more stable. It obviously is not a straight line like the assumption, but the smoothing is doing its job. On page 9, so when look back to the September 1, 2013 valuation, the market value is actually lower than the actuarial value. So the smooth value of assets was higher than the actual market. That's not unusual. We expect that to happen about half the time. That difference was \$35 million. So there was what we would call deferred investment losses, deferred in they just haven't been recognized because the smoothing. With the experience we had fiscal year end '14 was a 13 percent return on market value that eliminated that unrecognized loss and actually created an unrecognized gain of \$17 million. So that means now the market value is higher than the actuarial or smooth value. And that was due to the 13 percent return. The next page, 10, shows you the actual numbers for market and actuarial value of assets and how we went from the values in September 1 of '13 to September 1 of '14. Again, you'll see that flip from in '13 the actuarial being higher than market to the row that shows the assets, 9-1-14 which has the market value \$17 million higher than the actuarial value. And that 13 percent return on market translated to a return on actuarial value of about 8.5 percent. So the assumption is 8 percent, 8.5 percent would produce a gain. Page 11, again just to give you a little bit of a historical perspective on the actuarial and the market value, the red line is the actuarial value. The blue bars are the market value. And over a very long period of time, 30 or 40 years, we would kind of expect the actuarial value to be higher than market half the time and lower half the time. We don't have that long of a period here, but you can see there were certain points in time where the market was above actuarial value. The next page, 12, is really kind of the nuts and bolts of the valuation results.

SENATOR KOLTERMAN: Can we go back to that last page?

PATRICE BECKHAM: Sure.

SENATOR KOLTERMAN: So what you're telling us in essence is the market value has only exceeded the actuarial value in 3 years out of 12, would that be correct?

PATRICE BECKHAM: Yes, it's been it's looks like I'd say equal to or greater than in four years. But again, you're looking at a short period and quite frankly a rather poor period...I mean a tough period...

SENATOR KOLTERMAN: Well, but 12 years is 12 years. I mean...

PATRICE BECKHAM: Well, I could pick 12 years in the 1990s and it would look a lot different. (Laugh)

SENATOR KOLTERMAN: Well, yeah. But...

PATRICE BECKHAM: I mean it was a difficult investment period was my point.

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

SENATOR KOLTERMAN: Okay.

PATRICE BECKHAM: But, yes, that's exactly what that graph shows.

SENATOR KOLTERMAN: Do you ever adjust the 8 percent up or down?

PATRICE BECKHAM: Well, that's...we do what's called an experience study every five years where we look at everything that's used in the valuation process: the methods, procedures, the assumptions. That would be one of the key assumptions. And the rate of return is evaluated to see whether we should keep it or recommend a change. So the actuary would make a recommendation to the board, and the board ultimately makes that decision.

SENATOR KOLTERMAN: Okay. Thank you.

PATRICE BECKHAM: Okay. So I think we're on page 12. So the first step in the valuation process is to calculate this first line, this present value future benefits, which is just, as I mentioned, looking at the potential benefit payments that could be paid to the current membership only--we're not looking at new hires, anybody coming in the future, just the current members--under every possible scenario--you know, termination of employment, preretirement, death, retirement--and the probability associated with that event and then putting that in terms of today's dollars. That's what the present value means. It's just a little over \$2 billion. If we had \$2 billion in the fund today and we didn't let anybody else join in the future and all the assumptions were met, we wouldn't have to put any money in, okay. That would cover the obligation. But we do have people working who we expect to actively continue to work in the future and there will be a piece of the cost of those benefits allocated to those future years of service. That's that second line, kind of funky wording, present value of future normal costs. But that just means for people that are going to...currently are employed on the valuation date and expected to continue to work in the future, we're funding this over their working career. So for future years, there's some money that's supposed to come in; that's what it means. So the difference between those two, which we call the actuarially accrued liability, is really kind of a past service liability in the sense that according to the theory that we're using for funding, that's how much should have accumulated in the asset pot for those years of service.

SENATOR GROENE: Chairman.

SENATOR NORDQUIST: Yeah, please.

SENATOR GROENE: The present value of benefits is an average, right?

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

PATRICE BECKHAM: No, it's not an average. For each person that would be in the valuation, we would look at all the potential benefits to be paid to that person.

SENATOR GROENE: But there's some folks that made \$200,000 and are going to get a lot more than \$2,000...

SENATOR NORDQUIST: This is plan total, in millions. So it's \$2 billion of...

SENATOR GROENE: Oh, all right. Present value of benefits.

SENATOR NORDQUIST: Yeah. Yep, yep.

SENATOR GROENE: I thought it was an average payment out (inaudible).

PATRICE BECKHAM: No, that's everybody all together, what's the total obligation for all future benefits. I'm sorry. I didn't explain that very well.

SENATOR GROENE: All right. Thank you. Not per capita.

PATRICE BECKHAM: So the past service liability, the actuarially accrued liability, about \$1.7 billion of the \$2 billion. And then we've accumulated an actuarial value of assets, \$1.3 billion. The difference between those two, the \$446 million just means there's additional funding that has to be made in addition to the money that's coming in for the people who are earning benefits in the future. It's a little bit like a debt of the system. As long as there's a funding source for that, it's not problematic. And then we often see funded ratio as kind of a key metric from the valuation, which is actuarial assets divided by liabilities because you get to working with these really big numbers. It's a probably better benchmark, so just over 74 percent funded in the '14 valuation. Page 13...

SENATOR DAVIS: And what was the bottom, when this was at the bottom? What was the lowest ratio that you had?

PATRICE BECKHAM: I'm not sure. Let me check.

SENATOR DAVIS: And what year was that?

SENATOR NORDQUIST: Oh, yeah, on the next...on page 14 there's the chart of the funded ratio.

SENATOR DAVIS: Okay. There we go.

PATRICE BECKHAM: It looks like...

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

SENATOR NORDQUIST: That was the high in '07. And '12, '13...

PATRICE BECKHAM: Yeah, it looks like maybe '12 in the table.

SENATOR KOLTERMAN: That's really odd that it would work that way.

SENATOR NORDQUIST: That's okay, Pat. The chart I think answers the question.

SENATOR DAVIS: That's okay. I see it.

PATRICE BECKHAM: You see it? Okay.

SENATOR NORDQUIST: Yeah.

PATRICE BECKHAM: So page 13, which just looks at that unfunded liability, that obligation of the system that requires additional funding source, how did that change from '13 valuation to the '14 valuation? Some of the change is expected, okay. It's being financed over a 30-year period with payments that are level as a percentage of payroll. The payroll is expected to increase. That means the dollar amount of the contribution increases. And over 30...when you do that over 30 years expecting payroll to increase, the payment in the early years doesn't even cover the interest on the debt, essentially. And so that went up, you know, \$10 million because of the amortization method. Again, that's not uncommon in public plans. And then the other significant ones, a decrease of \$6 million from investment experience. Remember we said the 8.5 percent return was greater than the 8 percent assumption. So that lowered the unfunded liability. There was...experience salaries were lower than they expected. So if the benefits are lower, the liabilities are lower. That was \$8 million. And then it had a liability loss on retirement. So it was more liability than what was anticipated from the assumptions. Those were the kind of key changes. So it went from \$455 million in the '13 valuation to \$446 million in the '14 valuation. Okay, slide 14, I guess that's what we were talking about earlier. On page 15, just to spend a minute to talk about the actuarial contribution rate, which is on the next slide, so there are two parts to financing a retirement system under the methodology that we're using. The normal cost is that theoretical amount that's needed from the point a person comes into the system, so date of hire, to the point that they leave the system. And it's calculated as a level percentage of payroll, okay. And that calculation is done for each person, each one of those 7,400 actives, and then added together to come up with the results. That's what we kind of call the ongoing cost of the system, okay. It is totally independent of the asset value. It reflects the benefit structure, the assumptions, and the membership, your census. That's all it's based on. And then you have the UAAL payment, which is to fund or finance that shortfall between the actuarially accrued liability and the actuarial assets. That's based on the board of trustees' funding policy. So again, the payments are calculated as a level percent of payroll, and payroll is expected to increase over the amortization period. And they

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

moved to a closed 30-year period beginning with the 2013 valuation. So in the '14 valuation, the amortization period is down from 30 to 29. And then when the '15 valuation comes, it will be 28. If you look at the next page, page 16, again, kind of laying the '14 results next to the '13 valuation results. We just talked about the normal cost. So it's just over 12 percent of pay. If you were looking kind of at the benefit structure given the set of assumptions, what's the value of the benefit again, on average for everybody in the group, it's about 12 percent of pay. And then the amortization piece is 8.21 percent. So the total actuarial rate is 20.23 percent. And that's again, based on that 29-year funding of the UAAL. If you look at the contributions, the member, employer, and the state together are putting in 21.66 percent. Okay, so right now there is what we call a margin. The money coming in is above the actuarial contribution rate.

SENATOR NORDQUIST: Can I just real quick, so if this is...just you can yes or no if this is the right understanding. Normal cost, if I'm an employee who starts today in OPS, it's going to take, assuming 8 percent rate of return, other longevity, salary, things are met, it's going to take 12 percent, 12.02 percent of contribution to pay for my benefits that I'm accruing today. But I'm...between me, the employer, and the state, we're putting in 21 percent. So the excess of that essentially is going to help pay off the unfunded liability.

PATRICE BECKHAM: Exactly.

SENATOR NORDQUIST: Okay.

PATRICE BECKHAM: Well done.

SENATOR NORDQUIST: Thank you.

PATRICE BECKHAM: Exactly. Yeah, when there's additional funds available, it automatically goes to pay down the unfunded liability. If you go to the next page, again, I think the second bullet there is a little bit of a follow up to Senator Nordquist's comment. And that is if we just took the valuation results, okay, which would assume that the amount available for the UAAL is the same over the next 29 years, the system would pay that off in 23 years instead of 29 years because of the additional...the margin. However, that ignores the fact that we have a second tier that is a lower cost. So the same amount of money coming in and the normal costs going down, we have more money over the years available to pay the UAAL. And then there's a...you know, there is that small deferred gain that is not recognized in that either. We can't really quantify that without doing what we call that open group modeling that you've seen the...the committee has seen the results of that before for the statewide system. So we can't say exactly when that happens. But it's certainly earlier than 23 years.

SENATOR NORDQUIST: So if we weren't to meet an 8 percent assumed rate of return year after year and it was lower than that, do you have any sense of what percent rate

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

of return we could still sustain the plan on for new members at the 21.6 percent? Let's say no money was going to pay the UAAL but just paying for the benefits that the...the normal cost for the new members, could this plan survive if we only were to return 7.5 percent moving forward?

PATRICE BECKHAM: Well, there's a lot of moving parts, and I don't have that off the top of my head. I might be able to...the thing is we still have this increasing payment for the UAAL. And without the open group modeling, you know, there's really not an efficient way to estimate that. But also remember that the system could go on even if it's not fully funded in 29 years or 23 years or 30 years. I mean...

SENATOR NORDQUIST: Sure. Right, right, because we're not closing the system tomorrow and have to pay off all those liabilities today.

PATRICE BECKHAM: Yeah. There could easily still be money to pay benefits, and it may hit full funding further down the road. Any other questions?

SENATOR NORDQUIST: Any questions from the committee? I just had one on...this is on one of the bills actually we have coming up. So this is...any other questions about the actuarial study here before...? Just if you can, Pat, I think there was some note on the fiscal note on LB448 on the merger bill that you kind of looked at. Just the process, the actuarial cost to consider a merger, you looked in Minnesota. I think you worked on something similar. Can you just kind of walk through what generally that would entail as far as what would be analyzed and what those costs would be.

PATRICE BECKHAM: Right, and some of it, you know, the bill is sort of open-ended about how it would be accomplished. We did work in Minnesota with the Teachers Retirement Association up there when Duluth merged in. Those benefit structures were identical other than the cost-of-living adjustment. And they basically gave the retirees the higher cost-of-living adjustment, and they just kind of folded them in. But a lot of analysis on how that gets funded, I mean the unfunded liability doesn't go away. And then in that case when they increased the COLA, it increased the unfunded. And the state was involved in making TRA whole. So the existing system didn't bear the cost of the merger. In Colorado, the Denver Public Schools Retirement System was merged into Colorado PERA back in 2010. And in that situation, they were merged in but they were a separate unit, like they're a single-employer plan under the umbrella of Colorado PERA. And so they have their own contribution rate. And new hires come in under the PERA benefit structure, but people from DPS stay under the existing structure. And so, you know, we don't have any idea which...how this merger would occur and whether it would be existing folks or just new folks. And if it's existing, are there changes to the benefit structure. There's a lot of questions to work through that could end up taking a lot of consulting time.

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

SENATOR NORDQUIST: I have one more question and then I'll take Senator Groene's. The one thing that still is different, the tier 2s on both plans still are not the same, that we do have slightly additional on a couple components of benefits, the medical COLA and the service annuity on the OSERS plan that is not...the base benefits are pretty much the same, but you have those two additional components on the OSERS plan. But you have the same fund contribution rates going into both plans now. If we're assuming the same rate of return on both but we're giving higher benefits on the back end for OSERS, are we just pushing off how long it takes to pay off...I guess how much money we have going to pay the unfunded liability because the normal cost I assume in OSERS is higher than the normal cost in the state plan. I haven't looked. I guess I should have compared on the actuarial study but of the two, what the normal cost is.

PATRICE BECKHAM: I looked at this morning. It's a little bit higher. It runs in my mind, maybe for the statewide system it's 11.8...where's Phyllis (phonetic)?

SENATOR NORDQUIST: Okay. That's something probably should look at.

PATRICE BECKHAM: She may know. But it's just slightly higher. But the state service annuity is a modest benefit. So the medical COLA would be the main difference.

SENATOR NORDQUIST: Okay.

PATRICE BECKHAM: And of course that's a set dollar amount and deferred, so it's not a particularly expensive benefit either.

SENATOR NORDQUIST: Right. Both those probably are not huge, right?

PATRICE BECKHAM: Right.

SENATOR NORDQUIST: Okay, great. Senator Groene.

SENATOR GROENE: Thank you, Chairman. In Denver, Colorado, and Minnesota, they blended the money though...

PATRICE BECKHAM: No.

SENATOR GROENE: ...and it was invested by the same investment council?

PATRICE BECKHAM: Okay, yes. All of the funds in Colorado, they have five groups. And all the money is invested by Colorado PERA. They're in separate trusts.

SENATOR GROENE: The money is separated though.

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

PATRICE BECKHAM: Yeah. So there's no mingling of the assets. So the money that goes in to fund Denver Public Schools is in their trust and used to pay benefits to their members only.

SENATOR GROENE: But proportionally they're probably invested the same way in both funds, or they don't try experiments with this fund and invest differently with the other funds?

PATRICE BECKHAM: I don't think so, but I can't speak specifically to that. And in Minnesota, on the other flip side, Duluth was just kind of folded in with all the rest of the TRA members.

SENATOR GROENE: All right. Thanks.

SENATOR NORDQUIST: Any final questions? Seeing none, thank you so much, Pat.

PATRICE BECKHAM: You're welcome.

SENATOR NORDQUIST: Is there anyone who would like to testify in response or generally to the actuarial study? Seeing none, that will close that component. I'm going to be turning the Chair over to Senator Davis here because I have the two bills. Can I just see, first of all, a show of hands for individuals testifying on LB448 which is the merger bill. I see three, four hands, okay. And a show of hands of individuals testifying on LB447 which is the governance structure. One, two, three, four, five, six, okay. We have about 50 minutes to get through both of these. We probably, at least for the first bill, won't use the light system yet. We'll just ask everyone to try to keep your testimony between three and five minutes so we can move along. Thank you.

SENATOR DAVIS: Welcome, Senator Nordquist.

SENATOR NORDQUIST: Thank you. Vice Chairman Davis, members of the esteemed Retirement Systems Committee, I am state Senator Jeremy Nordquist from District 7 in downtown and south Omaha here to introduce LB448. This bill was introduced to begin a discussion about merging the Class V plan, which is the Omaha School Employees' Retirement System, or OSERS as we've described it, merge that with the school employees retirement system. As currently drafted, the bill, LB448 would transfer all the current members of the Class V plan into the school employees retirement plan on or after an unspecified date. It would require all regular employees of the Class V District hired on and after an unspecified date to become members of the school employees retirement plan. Over the past several years, we have worked to make the systems more similar. Some of the changes have included we now have the same employee contribution rate at 9.78 percent, and employers match 101 percent of that. The state now contributes 2 percent of compensation to both plans. We created a second tier of

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Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

benefits for the system in 2013 for new employees. That tier of benefits includes a 1 percent COLA. We reduced the COLA from 2.5 percent to a maximum of 1 percent. And we moved from 3 years of final average salary to 5 years of final average salary. This year we passed a bill to model capping...put capping language in those final five years in the OSERS plan to be similar to the state plan. They're due...as I just mentioned in the previous hearing, previous...on the actuarial study, there are two differences still. And that is in addition to the regular COLA, OSERS members receive a medical COLA which begins 10 years after retirement, and then they get \$10 a month. For each year of retirement, it increases \$10 per year to a maximum of \$250...is that per year or per month? Month, okay. Clarify that, \$250 per month. And then the OSERS members also receive a service annuity. In addition to their regular annuity, the service annuity is paid by the state and is equal to \$3.50 per month times your year of service. One of the...I should say that the bill as it's drafted right would not be the bill as in its final form. I did come to our legal counsel with this idea on about Day 5 or 6 of introduction. And she said do you know how many sections of statute are affected by this? And I said, well, give it...at least state the case over...make it general, as general as we can to begin the discussion. So there obviously would have to be extensive amendment if the committee chose to move forward with a full merger. One of the ideas that I know I've talked to some of you about, we've been talking to a lot of interested parties about, is the possibility of exploring having Omaha, the OSERS plan contract with the Investment Council to invest the OSERS pension portfolio. We have gotten some information from OSERS on their plan assets, their portfolio and passed that along to the state investment officer. Obviously the state has very much...very much has a big stake in the game dollarwise when it comes to the OSERS plan with a 2 percent contribution rate. As taxpayers in Omaha, Senator Mello and Kolowski and I have a stake in the game and the taxpayers that we represent...well, I guess, Senator Kolowski, do you have any of OPS, I don't know if you do. [LB448]

SENATOR KOLOWSKI: No. [LB448]

SENATOR NORDQUIST: But at least Senator Mello and I have OPS students, teachers, constituents, obviously who pay taxes to the district, who have a significant stake in the health of this plan too. So that's why we are beginning this discussion. It probably needs a lot of discussion. And that's what we're starting today. And I'd be happy to answer any questions. [LB448]

SENATOR DAVIS: Any questions? Senator Nordquist, do we have any idea what that medical COLA is in terms of an annuitized figure? Is there a dollar figure out there? [LB448]

SENATOR NORDQUIST: I think we'd have to check with Pat Beckham after the hearing or follow up on what the additional costs. It's clear, as she mentioned, that there is some additional cost even for new hires coming into the system. The bill, you know, if we were

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

to do a full merger, obviously we would look at aligning the benefits completely so all new hires, whether you're hired in Millard or in Omaha, you would get the same benefit. Again, that would only be for new hires and obviously that's based on your pay, and as pay differentiates between districts across the state, you would still get a benefit that is based on what you're paid. So I don't think that that would create harm necessarily to the school employees. I think it would be a matter of fairness and makes a lot of sense to consider moving in that direction. [LB448]

SENATOR DAVIS: Thank you. Any questions? Senator Kolterman. [LB448]

SENATOR KOLTERMAN: Go ahead. Kolowski was first. [LB448]

SENATOR KOLOWSKI: Thank you. Appreciate it very much. Senator, on the negotiations between both parties, will there be a third party or a third person involved in that, or just let the two groups meet and try to negotiate out many points it looks like that have to come together on as far as final? [LB448]

SENATOR NORDQUIST: Right. If we were to move forward with a full merger, certainly I think we would have to be in the middle of that and engage because one of the unspecified pieces of the bill is who ultimately would take over the liability? Right now, we only have liability as a state for the state plan. And the OSERS plan solely falls on the taxpayers of OPS. And that's why I certainly come here being an advocate for the taxpayers in my district and in Senator Mello's district and all of OPS, because if we see another, if we...you know, it's not likely in the short term we see a significant stock market crash like we saw in '08 and '09, but we certainly could see slower or at least some fall off from the equity markets where they are today. And at that time, you know, the state could say look, that's your plan. We have nothing to do with it. And you taxpayers pay property taxes that take care of that while every other taxpayer in the state is essentially protected by the state to pick up that shortfall in the teachers retirement plan. [LB448]

SENATOR KOLOWSKI: And with the differences as far as where funding is available and how much they have within each program, would that be another piece? Can that be negotiated out so it's more equitable? The one is not carrying the other, all those kind of things. [LB448]

SENATOR NORDQUIST: Right. Well, I think if you align the contribution rates and the benefits completely, then I think there is a complete equity argument. I mean I think you've taken that issue off the table. There is an unfunded liability there that needs to be addressed and obviously right now the state plan is 83 percent funded; the Omaha plan, 74 percent funded. So you know, changes need to be made and that's why this beginning merger discussion is probably further off because to do that, you probably...it's probably tough to do a merger unless plans are better funded than they

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Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

are, at least from the state taking that on. [LB448]

SENATOR KOLOWSKI: Thank you for bringing it forward. [LB448]

SENATOR NORDQUIST: Yeah. [LB448]

SENATOR KOLOWSKI: Thank you. [LB448]

SENATOR DAVIS: Senator Kolterman. [LB448]

SENATOR KOLTERMAN: Thank you, Senator Davis. Senator Nordquist, is the \$446 million unfunded difference, so to speak, does that include the medical aspect to this? [LB448]

SENATOR NORDQUIST: Yeah. So that would be...the entire benefit package is included in that actuarial study. [LB448]

SENATOR KOLTERMAN: In that \$446 million? [LB448]

SENATOR NORDQUIST: Yeah. [LB448]

SENATOR KOLTERMAN: Okay. [LB448]

SENATOR DAVIS: Senator Groene. [LB448]

SENATOR GROENE: Thank you, Senator Davis. Is it mandated, or is there some reason why the contributions have to be the same for the state plan and the Omaha plan? If they're behind in Omaha, why don't they just up their contribution? [LB448]

SENATOR NORDQUIST: They would have to come to us to do that. It's set in statute, but they could. [LB448]

SENATOR GROENE: Why is that? We control the statute but we don't control their investments? [LB448]

SENATOR NORDQUIST: Right, so we set the parameters of the plan in statute. It's the way I guess it's been. I know some states, when I go to conferences and talk to other, some states have floating contribution rates that aren't set in statute, that are set by some nonlegislative function that control those on... [LB448]

SENATOR GROENE: The management of the fund? [LB448]

SENATOR NORDQUIST: Right. I don't know how that's handled...how that works when

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

you talk about changing benefits on somebody and the contractual nature of retirement, how they can change contribution rates on an ongoing basis. I'm not sure exactly how that works out. [LB448]

SENATOR GROENE: One question, as somebody outside of Omaha, what advantage is it to us in Lincoln County that we take on this? [LB448]

SENATOR NORDQUIST: I do think that, and there are probably people who feel both ways about this, by having a single system, you do eliminate the double-dipping issue that we would have now where people can retire from one plan and go to another plan and build that up where if you just had one system, you're in the system, your years of service accumulate just in that system and your benefit is what it is when you leave. So I think there is some public policy benefit in that aspect. [LB448]

SENATOR GROENE: Thank you. [LB448]

SENATOR DAVIS: Any other questions? Thank you, Senator Nordquist. [LB448]

SENATOR NORDQUIST: Thank you. [LB448]

SENATOR DAVIS: We'll now take proponent testimony, proponent testimony. Seeing none, we'll take opponent testimony, opponent testimony. Seeing none, neutral testimony. [LB448]

VIRGINIA MOON: In the interest of time, I'll be very, very brief. My name is Virginia Moon, V-i-r-g-i-n-i-a, Moon, M-o-o-n. Just about forgot how to spell my name here. I'm testifying for the Nebraska Council of School Administrators, and we're here to testify in a neutral capacity. I think that NCSA has a long history, especially Mike Dulaney, in terms of being involved in all of the discussions around the NPERS systems and how to keep it whole and good for all of our members. We certainly have members in both OSERS and NPERS, and so we have an interest in being sure that the plans are doing what they're supposed to do for our members and that they're sound so that our members can count on those for...going forward. But we are very interested in certainly being a part of those discussions as they go forward, as we begin to consider something as large as merging these two systems together. Any discussion that maintains those programs in a very fiscally responsible way is important to NCSA and our members. Any questions? [LB448]

SENATOR DAVIS: Thank you, Dr. Moon. Any questions? Seeing none, next proponent...next neutral testimony, sorry. [LB448]

JOHN LINDSAY: Thank you, Senator Davis, members of the committee. My name is John Lindsay, L-i-n-d-s-a-y, appearing on behalf of Omaha Public Schools. OPS is

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

appearing neutral on the bill simply because the bill as drafted is not a complete draft, just as Senator Nordquist explained. But we do support the continuing dialogue about looking to see what the future of OSERS should be. We're first committed to the stability of the plan. We want to be sure that our teachers and our staff and our retirees have a stable retirement plan in place. We do appreciate the efforts of this committee in trying to align the benefits, align some of the features of the two plans over the years. And we think those have been positive changes. And we appreciate the efforts of Senator Nordquist to look at areas where those alignments can continue when they make sense for the beneficiaries of the plan, when they make sense for the district, and where the board is committed to continuing this dialogue to look for other areas. We've had some preliminary discussions with Senator Nordquist about, and he talked them in his opening, about things like the investment function and where is that appropriately placed, not just for issues about expertise of investments, but things like if you have a larger number, can you reduce fees? Are there efficiencies that can be achieved by having one investment manager or...one board controlling those investments. And those are things we again, need to...it's all obviously complex stuff, big issues. So it's stuff that...things that we need to continue to have those discussions. We're committed to doing that if it does protect teachers, staff, current retirees and if we can achieve those efficiencies or if we can achieve those savings for taxpayers. With that, I'd be happy to answer any questions. [LB448]

SENATOR DAVIS: Thank you, Mr. Lindsay. Any questions? Seeing none, thank you for your testimony. Next neutral testimony. Any more neutral testimony? [LB448]

ORRON HILL: (Exhibit 3) Chairman Nordquist, acting-Chairman Davis, members of the Retirement Committee, my name is Orron Hill, O-r-r-o-n H-i-l-l. I am legal counsel for the Public Employees Retirement Board and the Nebraska Public Employees Retirement Systems. I'm here to testify to this bill in a neutral capacity. As has been stated, this bill is going to propose to merge the Class V schools employees retirement plan and the school employees retirement plan. In order to accomplish a merger of this magnitude, a legislative study would be needed to access and properly assess all the elements involved. An actuarial study and analysis would be needed to determine all the unfunded liabilities of each plan and how best to deal with any variance in those ratios. As has previously been said, NPERS is currently 83 percent funded and OSERS is 74 percent funded. Another issue of note is that NPERS has a June 30 fiscal year ending and OSERS has an August 31 fiscal year ending. The integration and implementation has a number of issues. I've listed examples of those issues for you in the written portion of the testimony that you can reference. To address those issues, NPERS provided a fiscal note that contained estimated costs. Of critical importance is the need for advanced funding in integration and implementation as current plans cannot fund the cost to integrate and implement this objective. One possible alternative that we would like to at least mention for the committee to discuss is the alternative that OSERS could become a seventh plan within the Nebraska Public Employees

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Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

Retirement Systems and have it be operated separately instead of merged into the school employees retirement system. Essentially, it would operated under the umbrella of the NPERS system, and over time it would give us the opportunity to explore whether or not that structure would be the best structure or if a full merger would be a better option--something to keep in mind. You've already heard from Cavanaugh Macdonald a little bit on this subject. They are responsible for both NPERS and OSERS. And we would be willing to work with them to get the best practices guidance to conduct any actuarial studies that would be needed. But we are definitely willing to work with this committee and OSERS to make that become the case if that's what this committee wants to do. One other note is that LB447 modifies a Class V school plan. And we would like to ensure that any pending modifications to either the Class V school plan or the school employees retirement plan be addressed prior to or during a merger of these two plans to ensure that we're getting a fair an appropriate assessment of all benefits across the board. The PERB did formally vote to testify neutrally to LB448 at the last board meeting. And I would be happy to answer any questions the committee may have. [LB448]

SENATOR DAVIS: Thank you. Any questions? Senator Groene. [LB448]

SENATOR GROENE: Thank you, Chairman. So if you bring it in as a separate plan into the Nebraska plan... [LB448]

ORRON HILL: Yes. [LB448]

SENATOR GROENE: ...now we're liable? [LB448]

ORRON HILL: We would still be liable. That is correct, yes. [LB448]

SENATOR GROENE: And that would be underfunded. And now instead of the employees who benefit in Omaha bailing it out, all of us are bailing out that separate plan even though my teachers in North Platte aren't getting anything out of that, right? [LB448]

ORRON HILL: That is one possible way. A lot of it would depend on how ultimately the committee and the Legislature pass the law into the nature of the legislation itself. But the thought is that it would come under the NPERS system. [LB448]

SENATOR GROENE: But came in the plan and kept it separate, could the Legislature then dictate to the OPS that they need to demand higher benefits to bail it out? [LB448]

ORRON HILL: The Legislature could certainly consider however it wanted to structure the plan during an integration. One consideration would be that if you're going to modify any of the natures of the contract of retirement--if you're going to increase costs or

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Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

change benefits--there is a contract theory, and I'm sure your legal counsel can speak to some more about how you can't violate that contract theory under some of the case law that's out there. But that's certainly something that would be part of the discussion, Senator. [LB448]

SENATOR GROENE: Thank you. [LB448]

SENATOR DAVIS: Other questions? Senator Kolterman. [LB448]

SENATOR KOLTERMAN: Thank you. Mr. Hill, can you...do we have the capabilities to manage the money as a state for the Omaha Public Schools, or would that have to be changed in statute as well...? [LB448]

ORRON HILL: Well, that's... [LB448]

SENATOR KOLTERMAN: ...because it's really an outside plan that we'd be managing the investments for. [LB448]

ORRON HILL: That's an excellent question, Senator. I think one of the reasons why this is being proposed, although I would certainly defer to Senator Nordquist, is that if we were to bring it as part of the NPERS system, we would then arguably then have the statutory authority to be able to manage the investments for it. That is certainly a concern that would need to be part of these discussions. [LB448]

SENATOR KOLTERMAN: But I'm just maybe...I guess what I'm asking, and I think you answered but I'm not positive I heard, could we...like if I had a plan and I wanted to bring it to the state and ask you to manage it for me whether it's city of Seward or city of York, do we have the legal authority to do that and charge to do that? [LB448]

ORRON HILL: Again, that's one of those specific aspects that would need to be discussed, Senator. [LB448]

SENATOR KOLTERMAN: Okay. [LB448]

ORRON HILL: There is certainly a question on that. And we would certainly need to see if just bringing the OSERS plan into NPERS would allow us to get there, or if we would actually have to do a full merger. That is part of this discussion, Senator, yes. [LB448]

SENATOR KOLTERMAN: Okay. Thank you. [LB448]

SENATOR DAVIS: Any other questions? So I've just got one question. Are there other states that are managing plans in this same way, that have a separate plan that's taken under the umbrella of the state plan? [LB448]

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Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

ORRON HILL: I can certainly do some research and get back to the committee on that. I don't know the answer for sure, Senator. [LB448]

SENATOR DAVIS: Okay. Thank you. Any other questions? Seeing none, next testifier. Is there any other neutral testimony? Seeing none, Senator Nordquist, do you want to close? [LB448]

SENATOR NORDQUIST: Real quick, and Senator Kolterman is walking out but I will say we have had discussions with the Nebraska Investment Council about the idea of management of the assets, even whether it's a merger or whether it's some other arrangement to manage those assets. And they, from initial discussions, say they would be very comfortable. And obviously we would have to establish in law that provision, but they would be very comfortable managing those assets. Right now they manage about \$12 billion or \$13 billion of our state pension assets. And this would be an additional \$1.2 billion I believe is what the actuarial study showed the assets to be, you know, a 10 percent increase. And quite frankly, the state investment officer said that additional money doesn't necessarily mean additional work for the people there, that the investment strategies and everything would align with their current work. And just, I talked to Pat real quick. So the Colorado system, Senator Davis, is where Denver is a separate system within that plan. So I'd be happy to take any other questions, otherwise I will open on our next bill so we can get moving on that. Anything else? [LB448]

SENATOR DAVIS: Any other questions? Seeing none, Chairman Nordquist, you're welcome to open on LB447. [LB448]

SENATOR NORDQUIST: Great. Thank you, Senator Davis, members of the committee. I'm going to keep my opening real short on this because I know there will be testifiers after me that can lay out, give a lot better historical perspective. But this bill relates to the governance of the OSERS plan, the board of trustees that oversees the plan, the makeup of that board that reports and is appointed by the Omaha School Board. And the bill would make a couple changes to that. First, it would remove the board of education members from the board of trustees and provide for the election of members of the board trustees by the members of the retirement system. Rather than having them appointed by the school board, they would be elected by the members of the system. It would place the retirement system administrator in OSERS and other retirement system employees under the control of the board of trustees rather than the school superintendent. It would create an independent investment authority for the board of trustees who make all the investment decisions regarding the system. Essentially, it creates a division between the board of trustees and the OPS School Board. Again, this bill is very much a discussion starter between all of the parties involved and trying to figure out what the right system is. At times I think about it like our state system where you have an Investment Council that invests our pension assets

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

and they don't have to come back to the Legislature or to the Governor for approval of the decisions they're making. But at the same time, the OPS Board is responsible to the taxpayers and any funding has to come...shortfall funding comes from the OPS Board. So I think what we're talking about here is the interaction between the school board and the board of trustees that are over the pension and what is that appropriate relationship. And as I said, there will be people testifying after me that can provide more detail about the history of that relationship, how things have changed and their thoughts on how we move forward. [LB447]

SENATOR DAVIS: Thank you, Senator Nordquist. Any questions? Seeing none, we'll take the first testifier. Proponent testimony on LB447. [LB447]

MARY MORRISSEY: (Exhibit 11) Senator Nordquist and Senator Davis and other members of the committee, good afternoon. My name is Mary Morrissey. For the record, my name is spelled M-o-r-r-i-s-s-e-y. I live in Omaha, Nebraska. I served on the Omaha Public School Board for four years, and as a member of that board I was also a OSERS trustee for two years. I'm here today to testify in support of LB447 which would make several changes in the governance of the model for OSERS. As a former OPS School Board member and a former trustee of OSERS, I feel that this bill will bring OSERS into a more modern governance model that would provide for a single fiduciary board that would govern and provide oversight for the retirement system. While I served on the OPS School Board, I was asked to represent the board on the OSERS Board. The board meets half a day monthly, once a month. And at those meetings, we were provided with information that told us about the investments of the previous month. The updates were provided on the progress of our investments and then also updates were provided on the investments of the fund as a whole. The discussions were very detailed. Each month we would also focus on a specific type of investment that OSERS was using. For example, one month we might deal with fixed asset income. And we would have the managers of these different funds present who would be there to answer the questions that we would have. The OSERS Board were able to question the investment advisors on the performance over the past year of our investments and then also have an open discussion on what the advisors felt that our investments were going to do in the future, both in the short term for a year or so and in the long-term position looking out perhaps for ten years. Questions and open discussions on the investments took place each month. As a person not trained in investment theory, the experience was very enlightening and daunting. There was a very steep learning curve to get up to speed on the investment terms. My background was not in investment theory or in managing a defined benefit retirement plan. As a result, I and all the other OSERS members had spent considerable time in training each year provided by the National Council on Teacher Retirement to acquire new knowledge, to refresh and hone the skills that we would need to be productive members of the OSERS Board. Investment recommendations that resulted from our discussion with our financial advisors and the OSERS Board are presented to the Omaha School Board. At that time...they were

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

presented to the Omaha School Board for final approval. The school board at that time gave great weight to the recommendations made by the OSERS Board, which had done all the due diligence on the investments and generally approved the recommendations without much debate. Having been a part of that two-step process, I've come to the conclusion that it is not in the best interest of the retirement system or its stakeholders. The OSERS Board has the opportunity to meet and discuss in great detail with our investment advisors what would be the best thing for us to do. The school board does not have the luxury of hearing all the discussion, all the details that went into the decision making that we had. Therefore, I feel it would be best if the final decisionmaking process would be left in the OSERS Board of Trustees. I would also support a smaller OSERS Board. I would also support the fact that the trustee members would be elected by the members. I would also suggest that they have their own legal counsel independent of the school district counsel. And I would also suggest that the OSERS staff report only to the OSERS Board of Trustees. The changes proposed in LB447 will not only provide a more efficient manner of governance for the retirement system, but it will also help prevent a conflict of interest that is inherent when final decisions are made by a board that has not fully participated in the research and the decision making process. Thank you very much for letting me express my opinion. And if you have any questions, I'd be happy answer them if I can. [LB447]

SENATOR DAVIS: Thank you, Ms. Morrissey. Any questions? Senator Groene. [LB447]

SENATOR GROENE: Did the board ever ask you to change an investment plan, the school board? [LB447]

MARY MORRISSEY: There were times, a few times when we brought a recommendation that it wasn't necessarily agreed to. There were questions on that. [LB447]

SENATOR DAVIS: Any other questions? Ms. Morrissey, I want to apologize for the lighting situation here. [LB447]

MARY MORRISSEY: Oh, that's okay. [LB447]

SENATOR DAVIS: You aren't the first person I've heard complain about that, and I'm going to take that up with the Capitol staff. [LB447]

MARY MORRISSEY: I have macular degeneration, so all the lighting you have is not going to make that much difference. (Laugh) [LB447]

SENATOR DAVIS: Well, it was just yesterday the same question came up with someone else. So thank you. [LB447]

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

MARY MORRISSEY: Well, thank you very much for your concern. Thanks. [LB447]

SENATOR DAVIS: I think we'll...in the interest of time, I think we'll start using the light system, and we'll go with go with three-minute lights. Next proponent, please. And I would remind you if you agree with the person that came before, just come up and state your name and say that last person stated it very well. Welcome. [LB447]

NANCY HUSTON: (Exhibit 12) Thank you. Senator Davis and members of the Nebraska Retirement Systems Committee, I am Nancy Huston. Huston is not spelled like the city; it is H-u-s-t-o-n. I live in Omaha. I am here today to testify in support of LB447, which would make several changes in the governance of the Omaha School Employment Retirement Systems, OSERS. I served on the Omaha Public Schools School Board for 16 years ending that tenure in December of 2012. It was a service I was pleased and proud to offer to Omaha. I ran for the board of education because I cared for public education. Having taught in the Omaha Public Schools, I was aware of the challenges faced by the teachers in the classroom. I understood teaching. I worked to continue to improve the schools in that system. And I knew that the responsibilities of the school board--not the just the Omaha Public Schools School Board but all school boards--were to hire and fire the superintendent and that included evaluation of that person's performance; to approve the budget for the system; and to develop, establish, and approve policy. Learning of the details and the work that is needed to keep the operation running smoothly was time consuming. I worked to keep myself current in the management of that system. As I learned more of the finer points of the operation of the system as large as the Omaha Public Schools, I began to learn of the work of OSERS. The reports that were brought to us involved the work of that board, a board composed of investment and legal advisors as well as representative members from the organization that benefit from the investments of those dollars. I was not an expert in managing a retirement system, but we as members of the board of education were required to vote on that board's recommendations. I trusted the experts who served on the OSERS Board, giving great weight to their recommendations. I did not have the expertise that they had spent in dealing with the recommendations they brought to us. I believed then and believe now that coming before the...OPS Board was an unnecessary step. I trusted the work of the OSERS Board. And I'm going to skip then to the end of presentation. They should have the authority to make final decisions for the retirement system. I, therefore, support the changes to the way that OSERS is governed that are contained in LB447. And I will be happy to answer any questions. [LB447]

SENATOR DAVIS: Thank you very much, Ms. Huston. Any questions? Seeing none, thank you for your testimony. [LB447]

NANCY HUSTON: Thank you. [LB447]

SENATOR DAVIS: Next proponent. And you understand how the light systems work.

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Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

We're a three-minute light. So you'll have two minutes with the green light. And the yellow is your caution light. And then red means you need to wrap it up. Welcome, sir. [LB447]

ROGER REA: (Exhibits 13 and 14) Thank you. Senator Davis and members of the committee, for the record, I am Roger Rea, spelled R-e-a. I live in Omaha. I'm a trustee of the Omaha School Employees Retirement Systems, but I'm also president of NSEA Retired. And I'm here today in that capacity, to represent my members from the retirement system in Omaha. As you know, the Legislature changed the composition of the OPS Board of Education about two years ago. The bill (inaudible) to reorganize the OPS Board was passed in February of 2013. A primary election was held in April of 2013, with a general election held in May. In a very short period of time, virtually the entire board of education was replaced, a new superintendent was hired, one who had no previous experience with the retirement plan, and brand new inhouse attorney was hired by OPS, again, one who had now prior experience with the retirement plans. In a few short months, almost all of the institutional memory that OPS had for the way that OSERS had been managed was lost. A significant reason for the past successes of OSERS is that the OSERS administrators and board of trustees were allowed to operate as an independent organization. Although state law put the final authority with the school board, as a practical matter in the past, the decisions that the...affected the retirement system were made by the OSERS trustees, trustees who fully participated in the due diligence process required to make those decisions. And the board of education merely ratified their recommendations. With the loss of institutional memory about the way that the system was managed, the easy path was to take a more literal interpretation to the language of the state law, which gives final authority for the retirement system to the board of education. If the school board makes final decisions without doing due diligence, it puts those decisions at risk for being driven by political agenda rather than being made by fiduciaries whose sole loyalty is to the members of the retirement plan. Having decisions made about the retirement plan made by the school board level is not a good governance model, and that's one thing that needs to be changed. LB447 makes the changes required to create a desirable arms-length relationship between the employer and the retirement system. An arms-length relationship helps ensure that the retirement system will have as its sole focus to do what is in the best interest of the members of the retirement plan. That is the fiduciary duty of any trustee. That's what members of OSERS need. And that's what they deserve. LB447 concentrates the power to make decisions about the retirement plan with those who have demonstrated an interest in learning about their fiduciary duties, namely their trustees. The current governance model which gives the final authority to the board of education, is not a model based on good governance. It's a model based on who has the power. And power is easy to abuse. An illustration of that abuse of power occurred last month. Last month the OSERS Board passed a motion directing the OSERS administrator to come here and testify in a neutral capacity on the impact the bill would have on the operation of the office. Last night, I learned that the OPS

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Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

Board officers told him not to testify on LB447 in any capacity. They did that not by taking action in public meeting, by simply taking advantage of what they deem as their authority to overturn or ignore any decision the OSERS Board makes. OSERS staff should not have to serve two masters. OSERS staff should report to the board that pays their salaries, which is the OSERS Board. I submit that the OPS Board of Education abused its power in the instance I cited. I ask that you take that power away from the board of education and return it to the OSERS trustees. OSERS is not broken, but its governance model is. I ask that you make the governance model for OSERS the same as the governance model for any retirement system in the state, in the nation and pass LB447. Thank you. [LB447]

SENATOR DAVIS: Thank you, Mr. Rea. You did that very well. (Laughter) Any questions? Seeing none, we appreciate your testimony. [LB447]

ROGER REA: Thank you. [LB447]

SENATOR DAVIS: Next proponent. [LB447]

JOHN JENSEN: Senator Davis, members of the committee, I'm John Jensen, J-o-h-n J-e-n-s-e-n. I represent the Omaha Education Association-Retired. When I was still actively teaching, now 12 years ago, I served as president of the National Council on Teacher Retirement--that's NCTR--and I was a 24-year trustee of the retirement system OSERS. NCTR members are state and local pension systems throughout the country of public school teachers and other school employees. Today the assets held by members of NCTR exceed \$3 trillion. I'm here to tell you that OSERS today is an extreme outlier compared to other public employee retirement systems throughout the United States. I learned that fact through conversations with other trustees and pension administrators across the nation and through numerous educational conferences over those 24 years that I was a trustee. And it's not just my opinion. I worked closely with the staff of the National Education Association, and major publication in 2008 called The Characteristics of Large Public Education Pension Plans. I know the lead compiler of that data, and she's a stickler for accuracy and spent over a year putting it together. Here are some of the select findings: 50 out of the 80 plans reviewed, or 62.5 percent of the plans had trustees who are members of the system elected by their constituent groups; nationwide, 79 percent of the plans are administered by the retirement system; administering a plan includes hiring the executive director, and in almost all cases, the legal counsel. In fact, I don't know of any case where it's not also in charge of the legal counsel. Only one plan, OSERS, has a board of education as the administering entity. Nationwide, 58 percent of the plans have assets invested by the retirement system. Only one plan, OSERS, has the board of education as the asset-investing entity. OSERS is also an outlier in another important area. The trustees' lawyer is the school district's lawyer hired by OPS, paid by OPS. The school districts counselor's duty of loyal is to board of education and not to members of OSERS. OSERS needs counsel

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

hired by OSERS, paid for by OSERS, and someone who is loyal only to members of the plan, no conflicts of interest, please. Senators, past boards of education always deferred to the trustees' judgment. There has never been a time other than last year and half when they did not accept any investment advice and recommendation. And that is not true today. There is conflict there. OSERS should not be such an extreme outlier. OSERS should be more like other public plans across the country. It's the right thing to do, and it works. I thank you, and I'd be happy any questions that you have. [LB447]

SENATOR DAVIS: Thank you, Mr. Jensen. You brought some great information. Any questions? I have one. The NCTR, is that what it's...the acronym? [LB447]

JOHN JENSEN: Yes. [LB447]

SENATOR DAVIS: So how are they investing funds? Whose funds are those that they're investing? [LB447]

JOHN JENSEN: The members of NCTR are the pension plans. So OSERS is a member. NPERS is a member of NCTR. Pension plans are members. [LB447]

SENATOR DAVIS: Gotcha. [LB447]

JOHN JENSEN: And the total assets of all those plans across the country is right at \$3 trillion. [LB447]

SENATOR DAVIS: Thank you, sir. Any other questions? Senator Kolowski. [LB447]

SENATOR KOLOWSKI: Thank you, sir. John, thank you for being here today. Good to see you again. How many people are on the board that make the investment decisions for the money in your program? [LB447]

JOHN JENSEN: OSERS? [LB447]

SENATOR KOLOWSKI: Yes. [LB447]

JOHN JENSEN: Well, currently there are ten trustees and ten people make that decision. [LB447]

SENATOR KOLOWSKI: Okay. Thank you. [LB447]

JOHN JENSEN: They use professional managers to do this, but when the manager comes and presents their case and OSERS makes a decision as to go with it or not. As soon as they make their decision, it goes to the board of education. [LB447]

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

SENATOR KOLOWSKI: Thank you. Appreciate that. [LB447]

SENATOR DAVIS: Any other questions? Seeing none, thank you, Mr. Jensen. Next testifier. [LB447]

JASON HAYES: Hi, Senator Davis and members of the Retirement Committee. For the record, my name is Jason Hayes, J-a-s-o-n H-a-y-e-s, and I represent the Nebraska State Education Association. We support LB447. Just as the Nebraska Public Employees Retirement System and the Investment Council are insulated from political pressures that may arise from one gubernatorial administration to another, we believe that OSERS should be independent from that same political process. Investment decisions and administration of retirement benefits should have continuity from one school board election to the next. And this is why an independent board is important. Also, the provisions in the bill pertaining to direct trustee elections would help ensure that teachers and classified staff have continued input on the management of their pension benefits and investments. We believe these are good reforms to help ensure greater independence on the part of the board of trustees to make informative decisions and will provide for a greater level of due diligence. And I thank you for your time. [LB447]

SENATOR DAVIS: Thank you, Jason. Any questions? Seeing none, next testifier. Any other proponents? Opposition testimony? [LB447]

LOU ANN GODING: Senator Davis and members of the Nebraska Retirement Systems Committee. My name is Lou Ann Goding, L-o-u A-n-n G-o-d-i-n-g. I am president of the Omaha Public Schools Board of Education and also serve as an OSERS trustee. The OPS Board is strongly opposed to LB447. Under current law, the OPS Board has ultimate responsibility for administration of OSERS. In doing so, we balance the best interest of our teachers and staff, and above all, our students. We also must be mindful of the taxpayers who elected us to office. The most significant problem with LB447 is the removal of elected officials from involvement with OSERS and replacing those elected officials with people selected by beneficiaries of the plan. The only outside oversight would come from outside trustees who were selected by trustees who are plan members. Those trustees would have absolute control over the purse strings and the OPS Board would be required to pay any contributions specified by the trustees. Discretionary decisions such as COLA adjustments for annuities would be transferred to the unelected board rather than residing with the elected school board as provided in current law. All administrative employees of OSERS would be employees of the school district with reimbursement made by OSERS. This would result in no check in place to control growth and administrative expenses. The school board would have no input into investment decisions or investment advisors. The incentive to maximize return would not be as strong with unelected board as it would be with elected school board because

of the school board's budgetary requirements. We find this approach extremely problematic. Imagine if this philosophy were in place at the state level. The Public Employees Retirement Board could direct the Legislature to fund whatever additional contribution it deemed necessary and the Legislature would have no power to question the judgment. The bill would essentially vest control over all aspects of the retirement system in the beneficiaries of the pension plan. We question whether there is a public pension plan in any place in the United States that is so structured. We take our fiduciary obligations to plan members very seriously. The minimum contribution required by law for the school district to contribute to OSERS is 101 percent. The law also imposes an obligation to contribute additional dollars when necessary for the solvency of the plan. OPS has contributed additional dollars over and above the minimum contribution because the board has determined that it was necessary to do so. While it is difficult to find those additional funds within an already tight budget, the board will find those funds when it deems it necessary. Before the bill was introduced, we discussed with the proponents the portions of the bill with which the school board could live. However, this bill ignored those discussions and went well beyond what we believe would be reasonable changes. Throughout the process, Senator Nordquist has been open and willing to discuss with us possible changes to OSERS. We are committed to continuing to work with Senator Nordquist and this committee, but LB477 (sic) is not the starting place for those discussions. We would urge the committee to indefinitely postpone LB447. I'd be happy to answer any questions. Thank you very much. [LB447]

SENATOR DAVIS: Thank you. Any questions? Senator Mello. [LB447]

SENATOR MELLO: Thank you, Vice Chairman Davis, and thank you, Ms. Goding, for your testimony. You mentioned an awful lot of components there. What really is the school board's main, driving opposition? Is it the fact that...I'm trying to assess if maybe what I heard you say is that you feel that the school board should have the final decision on anything regarding OSERS because the school board is...essentially fiduciary responsibilities lie with the school board, that's why? [LB447]

LOU ANN GODING: The school board holds the fiduciary responsibility and the taxpayers elected us to role of the school board so that we could ensure that, you know, we were taking care of not only the employees of the district but also the taxpayers. So ultimately the liability, which you heard earlier, rests with the school board and the taxpayers of OPS. [LB447]

SENATOR MELLO: Do you think one could make an argument though that to some extent the Legislature actually has the authority over all of this? And regardless of the school board's decisions, the Legislature can control OSERS on our own since we're the ones who...anything that involves essentially OSERS contributions and employer contributions rests with us. So thus, in theory, we make that decision, not you. [LB447]

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

LOU ANN GODING: You do. You do make the decision, correct, on many of those things. And that is in state statute, right. [LB447]

SENATOR MELLO: Okay. [LB447]

SENATOR DAVIS: Thank you. Any other questions? Senator Groene. [LB447]

SENATOR GROENE: But if it wasn't managed right, you would have to come up with the funds for the actuary to correct it, right? [LB447]

LOU ANN GODING: Correct. If the fund was not deemed to be appropriately funded, then OPS, the board of education would have to find the funds out of our funding sources to contribute toward the OSERS contribution. [LB447]

SENATOR GROENE: And I probably heard it but didn't catch it, but presently the board appoints members of OSERS? [LB447]

LOU ANN GODING: So the board does, and we've been very...we've taken the recommendations of those member groups who represent the OSERS trustees. So currently there's one retiree, two teachers which are certified, one noncertified staff, the two members of the public, three board of education members, and the superintendent then serve as the trustees. And each of those groups has recommended who they would want to serve, and the board has approved those. [LB447]

SENATOR GROENE: What's the term right now? [LB447]

LOU ANN GODING: So the term of everyone is one year, except for the public members which are three-year terms. [LB447]

SENATOR GROENE: Thank you. [LB447]

SENATOR DAVIS: Senator Mello. [LB447]

SENATOR MELLO: Thank you, Vice Chairman Davis. Ms. Goding, I guess I just want to revisit one component I just remembered of your testimony. You mentioned to some extent, you made an analogy in respects to the PERB Board or NPERS and the Public Employees Retirement Board operation, so to speak, outside of authority of the Legislature and telling the Legislature what we would have to do. Has the school board at all discussed the general processes the state has set in place in regards to a separate Investment Council, a separate NPERS Board that is appointed by a Governor, approved or confirmed by the Legislature and they do act independently, so to speak, where there's not...with the exception of a policy or a legislative law change operate outside of that political influence because that's something that you didn't really

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

address in your testimony, which is to some extent a school board, the school board members who may have political agendas, that try to influence investment decisions where the Legislature on behalf of the state in all investment plans dealing with NPERS and the Investment Council is walled off from significant political influence. We even have it in state law where we can't make investments based on any kind of outside social benefit considerations. Is that something that you've at least discussed with your fellow board members is how do you take, for an example, what the state does and try to wall off that political influence, so to speak, that seems to exist or is able to exist at the local level? [LB447]

LOU ANN GODING: We haven't had that discussion in detail. I mean I understand that issue, and I think the political component could be at the trustee level or it could be at the board of education level. I don't know that it's just the board of education level. This particular bill would say that the trustees would tell the OPS Board what the contribution needs to be. And if we didn't follow that, we would have a Class V Misdemeanor against each of us for not complying. So that's a pretty significant issue for someone running for an elected office. [LB447]

SENATOR MELLO: I understand. Thank you. [LB447]

SENATOR DAVIS: Thank you, Ms. Goding. [LB447]

SENATOR GROENE: On more question, does the election...I could ask Senator Nordquist, but this election would eliminate any taxpayers on it, right? It would only be underlying membership groups. [LB447]

LOU ANN GODING: The membership...according to this particular legislation, yes, the membership groups would select... [LB447]

SENATOR GROENE: So the taxpayers who put in half the contributions wouldn't be represented. [LB447]

LOU ANN GODING: That's correct. There are two public members that serve but... [LB447]

SENATOR GROENE: On this board, on the... [LB447]

LOU ANN GODING: Right, that are business community members. But those would be selected by the trustees. So once again, you know, that would call into question the taxpayer component. And that's what the board of education is very opposed to. We represent the taxpayer as well. [LB447]

SENATOR GROENE: I want to thank you for being here. It's nice to see an elected

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

president of a board actually come and represent the people instead of employee.
[LB447]

LOU ANN GODING: Thank you very much. [LB447]

SENATOR GROENE: Thank you. [LB447]

SENATOR DAVIS: Thank you, Ms. Goding. [LB447]

LOU ANN GODING: Thank you. [LB447]

SENATOR DAVIS: We have about seven minutes left. So who has not testified that wants to in a neutral or an opponent status, would you raise your hand, please. Mr. Bonaiuto, I guess you're the last one. [LB447]

JOHN BONAIUTO: Senator Davis, members of the committee, John, J-o-h-n, Bonaiuto, B-o-n-a-i-u-t-o, representing the Nebraska Association of School Boards testifying in opposition to LB447. And our appearance here is to support the Omaha School Board in furthering these discussions. We appreciate Senator Nordquist introducing both of these bills which are important bills for future discussions. Obviously both bills are a work in progress and we believe the interaction between the Legislature and the Omaha board is critical. And knowing that there is that piece where the taxpayers are electing the school board to do certain things. And they have a fiduciary responsibility. And if there's a shortfall or...it's a unique system. And so having the school board be part of the future of this system is very critical and finding common ground so the taxpayers are well represented in the Omaha area. So NASB believes that both bills should be held in committee. And with that, I will end my testimony. [LB447]

SENATOR DAVIS: Thank you, Mr. Bonaiuto. Any questions? (Exhibits 4-10) I should read into the record letters of support for LB447 from Cheryl Richardson, president of the Omaha Education Association-Retired; from Ronald Gasper, craft and trade workers of Omaha Public Schools; from Walta Sue Dodd, retired educator from OPS; from David Knutson, former member of OSERS Board; from Alan Bolas, craft committee members representing OPS, Ron Gasper, Sam Schramm, Terry Grindstaff; Carolyn Grice, president of Omaha Administrators Education Association; and Terry Moore, president of Omaha Federation of Labor, AFL-CIO. Senator Nordquist, would you like to close?
[LB447]

SENATOR NORDQUIST: Yeah, I'll just say that obviously these two bills are very much intertwined. And how this committee chooses to move forward with the idea or alignment of the plans, the functions of the plans that are maintained at the local level versus the state level obviously impacts what the governance structure should be. And we will just continue this discussion with all the interested stakeholders and with this

Transcript Prepared By the Clerk of the Legislature
Transcriber's Office

Nebraska Retirement Systems Committee
March 05, 2015

committee. And hopefully we can find the right way forward. I'd be happy to take any final questions. [LB447]

SENATOR DAVIS: Any final questions for Senator Nordquist? Seeing none, thank you for your testimony. This will conclude the hearing on LB447 and the hearings of today. And thank you all for coming. (See also Exhibit 15) [LB447]