[LB219]

The Committee on Nebraska Retirement Systems met at 12:00 p.m. on Tuesday, January 31, 2017, in Room 1525 of the State Capitol, Lincoln, Nebraska, for the purpose of conducting a public hearing on LB219. Senators present: Mark Kolterman, Chairperson; Brett Lindstrom, Vice Chairperson; Kate Bolz; Rick Kolowski; and John Stinner. Senators absent: Mike Groene. [LB219]

SENATOR KOLTERMAN: Good afternoon. Welcome to the Nebraska Retirement Systems Committee hearing. My name is Senator Mark Kolterman. I'm from Seward and represent District 24. My committee members are, on my immediate left, Senator Brett Lindstrom from Omaha, District 18; my far right, Senator Kate Bolz, Lincoln, District 29; my immediate right, Senator John Stinner, District 48 from Gering. Senator Groene and Senator Kolowski will be joining us, I think. But if they don't we already have a quorum. My committee legal counsel is Kate Allen who will be introducing the bill for the committee today. My committee clerk is Katie Quintero and our page is Bobby. We're here today for the hearing on LB219. To better facilitate the proceedings, I would ask that you abide by the following procedures. Please silence or turn off cell phones. Those wishing to testify should come to the front of the room, be ready to testify. We will start with proponent testimony, then opponent, and finally neutral testimony. Please complete the blue sign-in sheets. And please state and spell your name as you come forward. If you have sign-in sheets that you want to just give us or information you want to give us that's read into the record, we'd be glad to accept that. With that, I would just ask how many are here to testify in support. And anybody here to testify in a neutral or opposition? All right. Okay. Ms. Kate, would you please open for us. [LB219]

KATE ALLEN: Sure. Good afternoon, committee members. My name is Kate Allen; that's spelled K-a-t-e A-l-l-e-n, and I'm the legal counsel for the Nebraska Retirement Systems Committee and I'm here to introduce LB219 on behalf of the committee. This is a bill that was introduced at the request of the Public Employees Retirement Board as a result of the 2016 actuarial experience study that was conducted on the state-administered retirement plans last summer. In the experience study, the actuary recommended a number of actuarial assumption changes including lowering the defined benefit plan investment return rate from 8 percent to 7.5 percent and the cash balance investment return rate from 7.75 percent to 7.5 percent. The actuary also recommended updating the mortality table from the current statutorily required 1994 mortality table. These new actuarial assumptions require statutory changes to all of the retirement acts. LB219 amends the definition of actuarial equivalent to clarify that judges, State Patrol, and school defined benefit plan members hired prior to July 1, 2017, will continue to have determinations based on the 1994 mortality table and the 8 percent annuity rate. For defined benefit plan member hired on or after July 1, 2017 or a plan member who is rehired on or after July 1, 2017, after termination of employment who is receiving a retirement benefit or who has taken a refund of contributions, the determination shall be based on the mortality table and annuity rate recommended by the actuary and approved by the Public Employees Retirement Board following an actuarial experience study, a benefit adequacy study, or a plan valuation. The July 1 date is used because the defined benefit plan year begins on July 1 of each year. For a state or county cash balance plan member hired prior to July 1, 2018, the 1994 mortality table will be used for converting the cash balance member account. For a state or county cash balance plan member hired on or after January 1, 2018, or a plan member rehired on or after January 1, 2018, after termination of employment who's receiving a retirement benefit or who has taken a refund of contributions, the mortality assumption used to convert the member cash balance account will be the mortality table recommended by the actuary and approved by the board following an actuarial experience study, a benefit adequacy study, or a plan valuation. The January 1 date is used because these plan years are based on the calendar year. LB219 also clarifies that the interest rate of return is recommended by the actuary as adopted by the PERB may be the rate used to calculate annuities for state and county cash balance members. We were advised yesterday by the...that the actuary has suggested several changes to the language in the bill. I'm working with Phyllis and Orron to draft amendments to accommodate those changes. They are here today and will be able to go into greater detail about the specifics of the bill, the impacts of the assumption changes and will also be able to explain the concerns the actuary has expressed when she was asked to review the bill and the substance of the proposed changes. I would answer any questions. [LB219]

SENATOR KOLTERMAN: Are there any questions for Kate? All right. [LB219]

KATE ALLEN: Okay. Thank you. [LB219]

SENATOR KOLTERMAN: Proponents. For the record, let it be known that Senator Kolowski is here. [LB219]

PHYLLIS CHAMBERS: (Exhibits 1 and 2) Good afternoon, Chairman Kolterman and Retirement Committee members. For the record, my name is Phyllis Chambers, P-h-y-l-l-i-s C-h-a-m-b-e-r-s, and I'm the director of the Nebraska Public Employees Retirement Systems. On behalf of the PERB, the Public Employees Retirement Board, I'm here to testify in support of LB219. And I would like to thank Senator Kolterman for introducing this bill and for Kate for doing such a great job explaining it the opening. In 2016, as was mentioned, the PERB conducted an actuarial experience study on all five plans. The statutes require us to do this every four years. The actuaries analyze the existing assumptions and determined that over the period from 2012 to 2016, the economic and demographic assumptions should be changed to reflect the experience of the plan. These assumptions are used directly in the annual actuarial valuations to assess the financial status of the plans and develop the actuarial contribution rates. The PERB approved the recommendations of the actuary but did not make those changes effective for the current plan valuations. Instead we went ahead and calculated the valuations this year on the previous assumptions that we were currently using. So the current statutes tie the valuation interest rate for the cash balance plans to the annuity factors. So immediate implementation would have decreased the benefits of members retiring after January 1 of 2017 if we were to have implemented them right away. After three public meetings receiving input from the Retirement Committee and the administration, the PERB approved the changes to the assumptions effective for July 1 of 2017 for the DB plans, and January 1, 2018, for the cash balance plan. The current mortality tables for benefit calculation purposes are expressly stated in statute. NPERS plan members are living longer and it is appropriate to reflect this fact in the benefit calculations. LB219 allows the PERB to change the mortality tables and the assumptions based on recommendations from the actuary following an actuarial experience study, a benefit adequacy study, or a plan valuation without having to go to the Legislature each time a change is needed. This is a practical change that will ease the burden, the administrative burden of timely implementing the changes to the actuarial assumptions for the actuarial factors. According to our actuaries, most state retirement plans that they consult with have this flexibility and are not locked in to statutory language. The mortality tables and the interest rate are the two key assumptions used in determining the actuarial factors for converting the base annuity benefit to an actuarial equivalent amount. The PERB is concerned that some members' retirement benefits might be affected by changing the mortality table. LB219 allows the PERB to keep the existing 1994 group annuity mortality table using a unisex 50 percent male, 50 percent female for converting the actual equivalent benefit for state and county plan members hired prior to January 1 of 2018. LB219 will allow the mortality tables to be changed for the new members hired on or after January 1, 2018. LB219 does not tie the cash balance interest rate to the investment assumption rate for purposes of calculating the annuity benefit. If this change is not made, there will still be timing issues of implementing assumption changes for valuation purposes because it will impact members' benefits. Under the proposed bill, the actuary's recommendation to the PERB could be implemented at an administratively convenient time without impacting the use of the assumptions in the actuarial valuations. If the Retirement Committee wants the cash balance interest rate and the investment rate assumption to be the same, you might consider the impact on current members when the change goes into effect on January 1, 2018. The benefit would be lower. The actuaries use assumptions in the valuation process to determine information about the future benefit payments including when, how much, and how long they will be paid. It's important that the assumptions are not too conservative nor too aggressive--in short, the best estimate to help predict the costs, the liabilities of the plan over time. The new assumptions that would impact benefit calculations have previously been stated, but they are the investment return assumptions which were lowered from 8 percent to 7.5 percent for the defined benefit plans and the school, judges, and Patrol and from 7.75 percent to 7.5 percent for the state and county cash balance plans. The most significant change in the experience study was the mortality...was the change in mortality assumption for all plans, a decrease in mortality that resulted from members living longer. I brought some examples for you to look at so you can kind of see what a benefit estimate is. If a member goes on-line or if we calculate a benefit estimate for someone retiring. I brought an example of a school plan and a state plan for you to look at. And what these show are you...the member or the retirement specialist would input the type of benefit it is, what is their age. We need to know they're going to live. We need to know how long their...if it's a joint and survivor, we want to know how long their survivor will live and what their age is. We also need to know what their estimated total service credit is for school plan and what their the estimated average salary is based on their three highest years of salary. And we also...so in this first one that's on top, this is a school plan member who is age 60, born in...with 30 years of service credit. And their average of their...the average of their three highest years of salary is $48,000 so their estimated average salary monthly is $4,000. Now roughly if you use the benefit formula for the school plan which is the final average monthly salary times the years of service of 30--so $4,000 times 30 years of service--times 2 percent, you're going to get $2,400 which is the gross benefit for option 3, five years period and certain. It would be the third benefit there. And that is the one that's in statute, the five year period and certain is our base benefit that we calculate from. Then all of these others, different options, whether it's a life only, a modified cash refund, a 10 year period certain, 15 year period certain, whether it's a joint and survivor 50 percent, 75 percent, or 100 percent are all calculated, the actuarial equivalent based off of the assumptions and the mortality tables that the actuaries use. And they provide us those factors which are input into our IT system and that's how we calculate the benefit and so you can see then the member can take their choice of which benefit option they would like to use when they retire in the school plan. The second choice, I've actually got two of them because one is with a COLA and one is without, but it's the state plan. And remember, the state plans are calculated based on the account value. So the account value is on the second page on the back. This one I put in $150,000. This person is again, 60 years old with an account value of $150,000 and they want to annuitize it. So the interest rate is very important, what that annuity is going to be based on because their benefit is directly affected by that annuity rate where the school is directly affected by the formula. And so that's kind of what we were talking about. If you change these interest rates, it directly impacts the state and county cash balance members. And again, they have the same benefit options. I would be happy to answer any questions that you have. [LB219]

SENATOR KOLTERMAN: Questions? I've got a few but... [LB219]

SENATOR LINDSTROM: I'll do one. [LB219]

SENATOR KOLTERMAN: Go ahead. [LB219]

SENATOR LINDSTROM: Thank you, Chairman. What direction did you receive from the PERB with regards to the provisions in this bill? [LB219]

PHYLLIS CHAMBERS: As far as supporting the bill? [LB219]

SENATOR LINDSTROM: Sure. Or just the provisions in here that they support, did you receive any direction as far as...? [LB219]

PHYLLIS CHAMBERS: Well, they are in full support of all of the... [LB219]

SENATOR LINDSTROM: Okay. All the provisions. [LB219]

PHYLLIS CHAMBERS: All of the provisions, yes. There weren't any that they had any exceptions to. [LB219]

SENATOR KOLTERMAN: I have a couple of questions, Phyllis. [LB219]

PHYLLIS CHAMBERS: Okay. [LB219]

SENATOR KOLTERMAN: But before we go there, I want to just say I'd like to thank Phyllis and Orron because we've worked on this a lot this summer and we had a lot of dialogue on all the bills that we're covering right now. So it's been great to work with them. For the sake of the committee, you've talked a little bit about how they can get their results when it comes time to retire. Is there any way that you guys are doing education about what these assumption changes might do to cash balance plans or will this have any effect on the current participants in the plan, other than the...after a certain date? [LB219]

PHYLLIS CHAMBERS: Well, based on what the Legislature does, we will certainly be informing our...the employees will have...we have our education services. And so that will be included in not only our newsletters, it will go into the handbooks and it will also go into our seminar presentations that we do. And the fall seminars will be for the state plan members, and then this spring we have the school plan members. So we do notify the employees of what is happening. We hope that their employers also send information to them and their employee groups, usually the union groups, etcetera, communicate with the members, too, hopefully. [LB219]

SENATOR KOLTERMAN: Okay. [LB219]

PHYLLIS CHAMBERS: Does that answer your question? [LB219]

SENATOR KOLTERMAN: It does, yeah. Does everybody have a clear understanding? The other question that I learned as we worked through some of this this summer is, would you talk a little bit about if you're in the cash balance plan, you have one extra option and that's to take a lump-sum distribution. [LB219]

PHYLLIS CHAMBERS: Yes. [LB219]

SENATOR KOLTERMAN: Can you give us any indication of how people take a lump-sum distribution in the county and state plans versus annuitizing the annuity that they could have. [LB219]

PHYLLIS CHAMBERS: Yes. Less than 10 percent of the members take an annuity. So a very small number of members take an annuity. We've seen an increase in the number of people. It used to be about 5 percent. So it's crept up a little bit over the last several years. But as for as...and part of the reason I think some of that, that there's fewer people who take an annuity is they have smaller account balances and they...so when you see the benefits, the monthly benefit is not a lot to live on. And then you have your Social Security. But, you know, for a lot of people who maybe aren't in state government for their full career, they may be having an annuity based on $30,000, $50,000. Keep in mind that state employees don't put as much into the plans as the other plans do. So their total contribution with the state and...with the employee and the state is only 12.5 percent going into the plans, so it doesn't grow...they're not putting as much in and it's not growing as fast. And one of the things that is on our calendar is an experience study this year, if we can work it in with the actuaries, to...I'm sorry, a benefit adequacy study so that we can, again, take a look at how many people are annuitizing and what kind of benefit are our people experience going through the cash balance plan. So there aren't a lot of people that take the annuity benefit. We see mostly people with higher balances, longer term career employees. Most of them do roll them over to an IRA and I think some of that has to do with whoever they are working with their financial investments, their tax accountants, or whatever their advisors offer to help them do their retirements for them. And so it is very liquid and portable and so whether they do a full career with us or partial career, it is that they are able to take their full...their employee contributions and their employer contributions when they take a distribution. One other thing I might add is that they are able to take a combination. So they can...it's not uncommon if somebody has a higher balance that they'll annuitize part of it and roll over part of it. Or they might take some cash out for an immediate need. So that they do have that combination that they can do with a cash balance and they can also...but it all has to be done at one time, whereas with the DC plan, the defined contribution plan, they can leave that balance in there and take partial distributions or systematic withdrawals. [LB219]

SENATOR KOLTERMAN: On the other hand, just so the committee is aware, when we talk about teacher retirement, the State Patrol, and the judges, they don't have a choice other than to take an annuity of the level that you look at here, is that correct? [LB219]

PHYLLIS CHAMBERS: They can take a refund, but for...in the case of the school plan members, they would only be able to take the employee portion. So they would be forfeiting half the value of their account which if they decide they're going to take money. Now it's been explained to me that halfway through your career is kind of the midpoint of when an annuity becomes more valuable. So early on if somebody is only teaching for five years or even less five years because then they wouldn't qualify for an annuity benefit, but it's...generally if those people leave and take another career or go somewhere else, they might take a distribution and just take their cash for their employee contributions, whereas somebody past 20 years, if they give up that annuity they're giving up quite a bit to take a refund and forfeit those employer contributions. [LB219]

SENATOR KOLTERMAN: Thank you. Any other questions? I just have one more question. But, Phyllis, would you talk a little bit because the committee doesn't really know how much we've worked on this type of legislation for the summer and during the interim, would you talk a little bit about how we came to drafting this kind of legislation and what goes into that. So you and I meet, and Orron and Kate and other people we also met with, the teachers and administrators and tried to come up with some ideas. Talk about how you involve--and we always use actuarial studies--how you involve your actuary, how Orron plays into this, how Kate, just so they have an understanding of how that all works. [LB219]

PHYLLIS CHAMBERS: Okay, well, as you said, this year we've...this is probably the busiest year I've spent working on legislation. Over the years I started off not hardly doing anything and mostly the legal counsel and the committee counsel did most of the legislation. And over the years I've gotten more involved. But also this...the last year or so, Senator Kolterman, you've been more involved and kind of by doing that you've brought together a lot of people where we were working with some of the unions--the NSEA, NACO, NCSA, the Nebraska Council of School Administrators. And so we have worked with those different employee groups. But we...what happens in our office is the benefit people say we're having issues with this, or Orron gets calls from schools right and left or...and a county calls us with an issue or we have an issue with a state agency. Those things come to our attention and as they get to us, we discover that there's an issue with those things and there might be a better way to make the administration of those issues, improve those issues, we bring those to you and to Kate. We do a lot with Kate. Talking to her, I know she spends a lot of time talking with Orron on the phone and walking through and talking through. When we go through the legislation, we're looking at line by line, word by word, as you know, everything has specific meaning and one little sentence can throw everything off as we've learned over the years. But we do work with a lot of different people.

Now as far as our board and the actuaries, it is very helpful having Cavanaugh MacDonald in Omaha to work with. And they are very accessible by the phone and I think both Pat Beckham and Brent Banister are very easy to understand, if you can understand the actuarial terminology and the concepts. They make it easier to understand. But they're very good to work with and very responsive and I think they've been very responsive to the committee for questions and studies and things that we've had. The board is very interested and appreciates the feedback from the Retirement Committee. We appreciate your willingness to look at our issues that we bring to you. And I think our board really wants to do the right thing. They want to be involved. They also recognize their fiduciary duty and they want to be representing all plans, not just their own plan that they...if they are specifically representing a certain group on the board. So it all works together and I think these kinds of things really help. [LB219]

SENATOR KOLTERMAN: Thank you, Phyllis. And as an example, so today we have this bill that was talked about. Whenever we make a change to the assumption, which we haven't done for quite a few years, according to statute we have to change statute and this will merely allow the PERB to work with the actuaries and make the proper changes going forward. And so every time, as interest rates are fluctuating like they are, every time we won't have to come in and change the statute to make the changes that are necessary to keep these plans solvent. With that, are there any other questions for the Director? Thank you very much. [LB219]

PHYLLIS CHAMBERS: Thank you. [LB219]

SENATOR KOLTERMAN: Is there anybody else here to testify in support of the bill? Anybody in opposition? Anybody neutral? Well, then that concludes our hearing. Would you like to close or do you want to waive closing? She's going to waive closing. (Laughter) So thank you very much, everybody. I appreciate you coming and spending time. [LB219]