

HOUSE COMMITTEE ON PUBLIC EMPLOYEE RETIREMENT SYSTEM

April 15, 2003 Hearing Room E
3:00 pm Tapes 50 - 51

MEMBERS PRESENT: **Rep. Tim Knopp, Chair**
 Rep. Alan Brown, Vice-Chair
 Rep. Deborah Kafoury, Vice-Chair
 Rep. Jeff Barker
 Rep. Tom Butler
 Rep. Greg Macpherson
 Rep. Dennis Richardson
 Rep. Wayne Scott

MEMBER EXCUSED: **Rep. Mary Nolan**

STAFF PRESENT: **Cara Filsinger, Administrator**
 Annetta Mullins, Committee Assistant

MEASURE/ISSUES HEARD: **HB 2003 – Work Session**
 HB 2008 – Work Session
 HB 2020 – Work Session

These minutes are in compliance with Senate and House Rules. Only text enclosed in quotation marks reports a speaker's exact words. For complete contents, please refer to the tapes.

TAPE/#	Speaker	Comments
Tape 50, A		
003	Chair Knopp	Calls meeting to order at 3:13 p.m. and opens work sessions on HB 2003, HB 2008, and HB 2020.
<u>HB 2003, HB 2008, AND HB 2020 – WORK SESSIONS</u>		
013	Chair Knopp	Announces that amendments are not available today.
	Jim Voytko	Executive Director, Public Employee Retirement System. Introduces staff.
	Voytko	Presents PowerPoint presentation on the statewide experience with the Defined Contribution Based on the Oregon Savings Growth Plan (OSGA) (EXHIBIT A).
075	Voytko	Continues presentation (EXHIBIT A, page 5).
088	Voytko	Continues presentation (EXHIBIT A, page 6).
102	Voytko	Continues presentation (EXHIBIT A, page 7).
117	Voytko	Continues presentation (EXHIBIT A, pages 8 and 9).
152	Voytko	Continues presentation (EXHIBIT A, page 10).
174	Voytko	Continues presentation (EXHIBIT A, pages 11-13).
202	Voytko	Continues presentation (EXHIBIT A, pages 14 – 18).
297	Chair Knopp	Asks if the number of participants is high on a national average.
	Voytko	Responds he was not able to get participation rates. The longer the employer has the plan in place, the higher the participation rate is. The participation rate has climbed since 1998 and believes if the program proves valuable to public employees, they will sign up.
	Chair Knopp	Asks what the limits are for contributions.
	Voytko	Explains that a federal law, EGTRA expanded the contribution

		limits, perhaps as high as \$15,000 per person that can be sheltered and it is pre-tax. Adds that that money is a substantial portion of the average public employee's salary compensation in Oregon. The law also combined and conformed the 457 structure with 401K so they look very similar. EGTRA also offered public employees certain catch-up provisions so there are extra deferrals they can make if they meet a certain age criteria.
340	Chair Knopp	Asks if there is data whether managers or others are using this vehicle.
	Voytko	Responds he does not have information. States that PERS does not ask for the occupation of any participants either in the basic PERS program or in the OSGP. Adds that with a 44 percent participation rate, most analysis indicate that administrators or managers are nine to thirteen percent. Even if every manager participated, they are outnumbered three to one by regular staff members.
	Chair Knopp	Asks if they know the salary range of the people participating in OSGP.
	Voytko	Responds they do not.
384	Rep. Macpherson	Asks Voytko to explain what Slide 5 (EXHIBIT A, page 5) tells us about the income replacement levels that are likely to be achieved under an elective plan based on the age distribution if we were to rely on an elective plan as the basic retirement plan.
	Voytko	Responds that the chart does not tell anything about how long an individual has been in the plan. Comments on age of workforce and age of participants, and desirability of the plan.
TAPE 51, A		
021	Rep. Macpherson	Comments it is the early contribution dollars that are important because of compounding.
	Rep. Macpherson	Comments that individuals tend to select a lower risk product than a professional manager. Asks what that means over the long term about the use of an assumed interest rate in projections—whether the eight percent over the long term is an appropriate rate to use for projecting what will be accumulated under a defined contribution program in which the participants make individual choices.
041	Voytko	Responds that he would not use the full eight percent that is used for a professionally managed pooled fund of assets; he would reduce that by one-half percent or one percent. Comments on investment strategies of employees.
059	Rep. Macpherson	Comments the choice is between having a plan with individual decision making by participants, in which, because of their natural risk aversion, will get a lower level of money at retirement than they would if they don't have to bear the risk, or having a system where the same dollars go in but the choice is taken away from the employee and they have no risk to allow them to get to a higher destination.
	Voytko	Responds that if Rep. Macpherson is talking about a defined contribution plan that is compulsory in terms of investment and that compulsory investment policy is based on higher risk, higher returns kinds of investment strategies that are more appropriate for pooled professionally managed investments, it would not be a good idea. That is because the employee would be subject to

088	Rep. Macpherson	<p>the higher risk, higher return strategies at all ages.</p> <p>Comments on investment options (EXHIBIT A, page 10). Asks if the OSGP is predominantly a mutual fund-based system, or whether there is a portfolio that is managed by the manager.</p>
	Voytko	<p>Explains these tend to not be mutual funds. Entry into the program is based on whether the money manager can produce an investment product that has the correct and competitive level of fees and fits one of the risk adjusted options that they want to offer to a member. It is merit based. PERS wants a bare bones fee structure, not a mutual funds fee structures.</p>
120	Rep. Macpherson	<p>Asks if they can compare the fee rates for management of the OSGP assets and the OIC portion for the PERS fund.</p>
	Voytko	<p>Responds they can negotiate attractive fees and even more attractive fees if they offer \$500 million or \$1 billion in a single package in a single account with no other record keeping requirement, other than the State of Oregon, for the consolidated PERS fund. Very few entities can negotiate fees at that level.</p>
136	Rep. Macpherson	<p>Asks for data comparing a typical manger in the big pool for PERS as to these providers.</p>
148	Rep. Butler	<p>Comments that the OSGP is managed separately and apart, neither providing resources for nor subtracting resources from the PERS system.</p>
	Voytko	<p>Responds that this is a separate program and bares all its own costs; it neither cross subsidizes nor receives a cross subsidy from the PERS plan, except to the extent that when knowledge is developed, like knowledge of money managers and their strengths and weaknesses, they capitalize on that for both programs.</p>
	Rep. Butler	<p>Asks what the cost is compared to PERS.</p>
169	Voytko	<p>Explains that simpler structures are much easier to out source. Because of the unique structure and complexity, the PERS plan is close to a market of one, even though they do out source certain pieces of it. Straight-forward defined contribution plans have many options. That is why they have been able to manage the OSGP with no extra FTE, perhaps one extra Treasury Department person who focuses on the OIC investment side.</p>
198	Rep. Dennis Richardson	<p>District 4. Provides update on amendments to HB 2020 (EXHIBIT B). States they are trying to accomplish a defined contribution plan that is patterned after a 401K, a plan that will be affordable and flexible for providing good benefits for public employees and be reasonable and predictable for the citizens and employers. The plan will apply to all new employees of the state as of July 1, except for legislators and judges. States that some of the key features have been changed to address the concerns raised last week. Reviews the revised proposal (EXHIBIT B).</p> <p>Explains they previously had proposed that this would be a dollar-for-dollar match where an employee who chose not to participate would receive no employment retirement contributions; they have decided that the employers will still be available to contribute six percent, but there will be an automatic base of three percent for every employee who is employed for more than six months.</p> <p>Reviews the contribution rates (EXHIBIT A, page 1).</p>

		Reviews vesting provisions (EXHIBIT A, page 1).
	Rep. Richardson	Reviews the retirement age (EXHIBIT B, page 1).
276	Rep. Richardson	Explains change relating to administration and investments. A determination has been made to have OIC use their experience and contracts they have negotiated for the OSGP and the PERS retirement plan.
292	Rep. Richardson	Responds to previous questions about investments. Comments on dollar cost averaging.
321	Rep. Richardson	Reviews the data on social security income replacement (EXHIBIT B, page 2).
348	Rep. Richardson	Reviews the yields (EXHIBIT B, page 3) under the defined contribution plan.
366	Rep. Richards	Asks what is being done about disability.
	Rep. Richardson	Responds he believes it is best to have disability negotiated separately and not be included in the retirement plan. In case of disability, the employee would receive the amount that is vested.
	Rep. Barker	Comments on diminution of 401K and 457 plans that is prohibiting employees from retiring.
	Rep. Richardson	Responds that it is true a defined benefit plan provides something that can be counted on that is affordable and does not go bankrupt. There is an inherent risk and someone must pay for the risk.
	Richardson	Reviews earning experiences by TIAA-CREF (SEE EXHIBIT C OF COMMITTEE MINUTES DATED APRIL 3, 2003).
TAPE 50, B		
013	Rep. Barker	Comments on changing performers in the stock market over the year.
	Rep. Richardson	Comments on the wisdom of having nine different pools to choose from.
030	Rep. Macpherson	Clarifies the revised contribution formula.
	Rep. Richardson	Agrees with Rep. Macpherson's clarification.
	Rep. Macpherson	Asks if any of the dollars in the plan can be borrowed under the loan plan.
	Rep. Richardson	Outlines the requirements for loans.
	Rep. Macpherson	Asks if the employee and employer dollars can be borrowed.
	Rep. Richardson	Responds he believes it applies to vested money.
052	Rep. Macpherson	Comments it sounds like the intention is to have the same ability to borrow as under the IRC rules.
	Rep. Richardson	Responds that is correct; they want to make it flexible under the rules.
	Rep. Macpherson	Comments on the assumption of the 2.5 percent pay increases. Asks if they ran the numbers with the four percent pay increase assumption, which is what the PERS system uses in their actuarial valuations.
	Rep. Richardson	Responds that he did not, but wishes he had.
077	Voytko	Comments that the actuarial assumption for pay increases, including merits, promotions, and all things that increase salary, is 4.25 percent. This assumption has been questioned by the local employers because it does not seem to be in concert with current circumstances and does not compare well with recent contract negotiations. The actuary did a presentation to the PERS Board showing, using actual local employer, the effect over the years in various time periods of combining the salary

		increases in contracts plus promotions and merit increases. He made a very convincing case that the actual numbers over an employee's life span is more like 4.25 percent. This 2.5 percent would be characterized as quite conservative based on the assumptions they use today.
089	Rep. Macpherson	Asks if pay is going up more than 2.5 percent, whether the percentage of pay replacement would be lower because the actual pay of the employer later in his/her career would be quite a bit higher than what is being assumed here.
	Voytko	Responds he does not think so because the percentage that is being put into the defined contribution plan is a percentage of that number. The replacement ratios probably would not change but the absolute income levels generated, the account values, would be bigger in nominal terms.
	Rep. Macpherson	Comments he believes Voytko is right as to each segment of a person's career but if the pay is rising more rapidly and those dollars that were put in when the person was paid \$30,000 rather than \$60,000 a year, the tendency to use an understated pay increase assumption is that we would not achieve these levels of income replacement. Asks if that is correct.
	Voytko	Responds this is just math and they can work it out. They would be happy to run the figures. They do not assume it is a curve linear function, but that it is linear. They will run the number with the 4.25 and look at the replacement ratios and answer the question directly.
137	Chair Knopp	Asks what the amendments will do to the optional retirement plan (ORP) for the Oregon University System and Oregon Health and Sciences University.
	Rep. Richardson	Responds that the plan will remain a separate plan. Clarifies that judges, legislators and OUS are excluded from this plan.
141	Chair Knopp	Announces that he is still working on amendments to HB 2003 and hopefully will have the amendments to HB 2020 by tomorrow, and that the amendments are available for the hybrid plan. Adds that he intends to ask the committee to move HB 2003 next week.
169	Chair Knopp	Closes the public hearings on HB 2003, HB 2008, and HB 2020 and adjourns meeting at 4:21 p.m.

EXHIBIT SUMMARY

A – HB 2003, HB 2008, HB 2020, presentation on OSGP, Jim Voytko, 18 pp

B – HB 2020, revised successor plan to PERS, Rep. Richardson, 6 pp