HOUSE COMMITTEE ON PUBLIC EMPLOYEE RETIREMENT SYSTEM

April 17, 2003 Hearing Room E
3:00 PM Tapes 52 - 53

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 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 52, A		
003	Chair Knopp	Calls meeting to order at 307 p.m. and opens a work session on HB 2003.
HB 2003 – WORK SESSION		
088	Margaret Hallock	Advisor to Governor Kulongoski. Presents proposal to reform the existing PERS system **(EXHIBIT A).**
149	Hallock	Continues presentation **(EXHIBIT A, page 4).**
266	Hallock	Continues presentation.
313	Hallock	Continues presentation **(EXHIBIT A, page 6).**
322	Rep. Butler	Comments that the ideas presented are good but he is concerned the long-term plan inches us out of the current difficulties over a long period of time. The idea that we might be able to recapture the over credited amount from 1999 by suspending the COLA to members who retired under the money match between 2002 and 2004 causes him to be anxious about how long that would take. Asks if the recapture has been demonstrated and how long it would take to recapture the over crediting.
348	Hallock	Responds they believe if the change in crediting were to be implemented and active member accounts were credited with zero, that would pay their portion of the over crediting. The question then is should the recent retirees who were also credited be asked to contribute. Adds that many people currently in the system think that basic equity would require some contribution from people who participated in what some call a windfall or an error. The COLA would be the contribution from the retirees who benefited in that window of time.

370	Rep. Butler	Comments that Judge Lipscomb did not call it a windfall or error; he called it a breach of fiduciary duty and a violation of law.
375	Rep. Macpherson	Comments that the proposal does not reduce the benefit of any member; it recovers amounts that have been over credited in the past by preventing further increases. Ask if that is a fair understanding.
	Hallock	Responds affirmatively.
387	Rep. Macpherson	Asks Mark Johnson, Actuary, how long it would take to work out of the deficit in the reserve account—how many years would the Tier I fixed accounts accrue zero in their accounts.
395	Mark Johnson	Actuary. Responds that a lot of it would depend on how quickly people retire. It could be four or five years before interest is credited.
414	Rep. Macpherson	Comments that the effect is that the people who are at or closer to retirement age have the opportunity, if they are inclined to retire, to avoid participating in the recovery of the deficit, and those who are further out from retirement would tend to share more.
426	Johnson	Responds that the proposal attempts to avoid that type of crack allowing someone to leave without sharing some of the pain. Refers to his letter to Hallock dated April 15, and reviews page 5 **(EXHIBIT B).**
TAPE 53, A		
038	Rep. Macpherson	Asks why they would not continue the suspension of the COLA adjustment for the person who retired longer ago to fully recover from the individual.
	Johnson	Responds that could be done. Adds that this proposed provision was patterned after a part of HB 2003.
055	Rep. Macpherson	Asks for comparison of Oregon's full formula retirement benefits with other public employee pension systems across the country.
063	Johnson	Responds the full formula is at 1.67 percent, times years of service, times final average of three years salary. Those are similar to a typical public employee retirement system. After a 30-year career the employee would receive 50 percent of their last three years average salary. The police and fire full formula is designed to replace 50 percent of their average final three years of salary. The only reason the multiplier is higher is the police and fire career is defined as 25 years instead of 30 years. That is typical across the country.
072	Rep. Butler	Asks if the first line in the first chart on page 5 **(EXHIBIT B)** reflects the full 1999 over crediting.
	Johnson	Responds it is rough. The Board credited 20 percent and the PERS calculation is what interest rate would have been credited had the PERS Board filled up the Gain and Loss Reserve and set up a contingency reserve; it is about eight or nine percent. Adds that his expectation is that the PERS staff will have to calculate this for each individuals because there will be a lot of individual characteristics.
080	Rep. Butler	Comments that it appears to him that very few people would restore to the program the amount they were over credited.
	Johnson	Responds that the only people that would totally restore would

		be those who retire this year.
111	Rep. Butler	States that this method of calculations is not fully recovering the over crediting and it certainly is not immediate. States those were two directives in the Lipscomb decisions.
128	Hallock	Comments that their proposal has individual calculation only for the retirees who benefited and retired; there is not an individual calculation for everyone else. They are assuming the new interest crediting mechanism would be their contribution to their financial stability and over crediting.
148	Rep. Butler	States that his concern is that people are calling in on a regular basis for estimates.
	Rep. Kafoury	Comments that Rep. Butler's concern is why this committee passed the bill to charge a fee for people who call repeatedly.
	Chair Knopp	Comments on inadequacy of the PERS computers.
166	Rep. Richardson	Comments on history of crediting member accounts and makes the analogy that member accounts have been given an advance and they will not be paid until the amount is paid back over a period of time. Believes that is the least disruptive.
	Hallock	Responds that their view is that Tier I member accounts should be promised that their regular account at the end of their career will grow at the long-term assumed rate compounded annually, but it doesn't necessarily have to grow at that rate each year. States they are mixing the 99 year and smoothing rationale.
212	Rep. Richardson	Comments he likes the term smoothing rather than dealing with an overpayment. Comments there may be a way it can be done sooner, perhaps less focus on individual calculations and more on general adjustments or rule.
224	Rep. Barker	Comments that the floor for some time would be zero and the hope is to get the eight percent back eventually.
	Hallock	States there really are two concepts. One is the over crediting and the particular year, and the smoothing over time. The promise is that at the end of the career, the account would have grown at the assumed rate, compounded annually.
	Chair Knopp	Comments that the only way we would add to the liability is if it is in the negative.
236	Johnson	Explains that the liability could still increase. There are two floors. Nobody will receive less than the full formula. We are talking about the interest crediting pieces. The second floor is the Tier I money match calculation will never be less than their account had it always been credited with the guaranteed rate. States that the combination of eliminating the six percent contribution going into the account, plus the prospect of no interest for several years accelerates the time for those who will remain in Tier I for a number of years until the time they get back to the full formula, back to the 1.67 times the years of service. HB 2003 just eliminated the six percent contribution. The purpose of that was to get members back to the full formula. By adding this mechanism on reserving for interest credits to that and diverting the six percent to a different plant accelerates the time when one comes back to the full formula.
260	Chair Knopp	Asks what the three proposals total.
	Johnson	Responds that the three cannot be combined. Refers to page 7 of the report **(EXHBIIT B).** This package with HB 2001 and

		2004 would reduce the unfunded actuarial liability by about $9.1 billion.
312	Chair Knopp	Asks if the proposal is in the $6.6 billion range.
	Johnson	Responds affirmatively.
	Chair Knopp	Asks if this proposal should be requested as proposed amendments to HB 2003.
	Hallock	Responds affirmatively.
312	Chair Knopp	Asks if they have an opinion on the call from five to 10 years that currently exists in HB 2003. States he would prefer that it be seven years.
336	Johnson	Responds that this proposal will eliminate the deficit reserve faster. Adds that he has not looked into how long that would take but can do that if the committee wishes.
	Hallock	Comments they agree it would be unfortunate to have a call in the next year or two and are in favor of extending it.
358	Chair Knopp	Thanks the witnesses for their proposal.
378	Sen. Tony Corcoran	District 4. Believes the savings in the proposal will get us where we intend to go. Commends work of Chair Knopp, Hallock, and Rep. Macpherson. Looking at this from the labor community, the numbers are stunning. Thinks it is the right thing to do.
394	Chair Knopp	Recesses the work session on HB 2003 and opens a work session on HB 2020.

HB 2020 – WORK SESSION

431	Chair Knopp	Notes the committee has the HB 2020-6 amendments **(EXHBIIT C)** and a Legislative Fiscal Statement on the HB 2020-6 amendments **(EXHBIIT D).**
420	Rep. Richardson	Presents the HB 2020-6 amendments **(EXHIBIT C).**

TAPE 52, B

	Rep. Richardson	Continues presentation of the HB 2020-6 amendments **(EXHIBIT C).**
044	Rep. Butler	Asks if this is a 457 plan.
	Richardson	Responds it is a 401A plan; the Oregon Savings Growth Plan (OSGP) is a 457. Comments on possibility of employee using both plans.
057	Rep. Butler	Comments we have seen information that employees are making fairly sizeable contributions the OSGP and if the trend continues it could reduce the social security tax on the employers.
066	Rep. Barker	Asks when an employee could start drawing retirement without penalty.
	Rep. Richardson	Responds it would be 57.5 years of age or earlier if the benefits are actuarially computed.
	Rep. Barker	Asks what the retirement age would be for public safety employers.
	Dave Heynderickx	Deputy Legislative Counsel. Replies that normal retirement age is 58 and police and fire is 55, or age 50 for a police officer with 25 years of service.
083	Rep. Macpherson	Comments that the proposal appears to be a 401A tax qualified plan, and since 401K allows employees to defer income on a pre-tax basis, asks if the intended result is that contributions would be after tax.
	Rep .Richardson	Responds that it is assumed that would be the case. It is their understanding that it is not necessarily the case. Presently, an Oregon Administrative Rule (OAR) allows the employer to

		deduct what is being contributed to the 401A plan so long as it is deemed paid by the employer. If it is from the employee, there is a problem.
124	Chair Knopp	Asks if contributions that are not being picked up by the employers are after tax.
	Rep. Richardson	Responds that is his understanding.
	Rep. Macpherson	Explains differences between contributions in this plan and in the hybrid plan (HB 2008-1 amendments). Does not believe the employee contribution can be picked up so it can be pre-tax. Notes a transition rule in Section 10 of the HB 2020-6 amendments that would allow for the continuation of the collective bargaining agreement. States that for those employees who are covered by collective bargaining and who have a picked-up contribution, it would remain pre-tax under this set of amendments until the expiration of the current bargaining agreement. Outside that situation all the member contributions would be after tax.
155	Dave Heynderickx	Deputy Legislative Counsel. Explains his understanding of when contributions are taxable. Adds that Section 7 (2) leaves some wiggle room on the issue of employer-paid contributions.
184	Rep. Macpherson	Comments he believes the only way to avoid having the contribution be after-tax would be by taking out the element of employee choice. As long as we have employee choice and it is a 401A qualified plan, it would not be possible for the employee contribution to be pre-tax.
	Heynderickx	Comments he is not sure how much the element of employee choice comes into it as far as the amount or whether to make a contribution. The tax provision that allows the pre-tax has to do with whether or not the employer elects to pay the employee contribution on behalf of the employee. States that he does not know of anything that conditions the ability of the employer to do that or having a mandatory employee contribution.
	Rep. Macpherson	Comments that his view is that these would be after-tax contributions except for the narrow transitional rule that relates to the pick up.
202	Rep. Macpherson	Asks if, in doing projections of replacement numbers, they plan to factor in the after tax character of the employee contributions. States that an after-tax contribution costs the employee an extra 30 to 50 percent of the amount the employee wants to pay in because he has to pay tax on the dollars.
	Rep. Richardson	Responds he has not considered factoring it in because it is based on a presumption he is not willing to go to. Both plans are based on 401A and it would be saying the only way to avoid the pre-tax problem is to have the employer pay more. Comments on the Internal Revenue Code (IRC) and OAR. States they are trying to qualify under the IRC so that the employer will have been deemed to have made payments but have it be handled as an accounting practice so that the employer does not have to be totally responsible for them. It can be done by adjusting income in other ways. They want to be sure that employers are not found in the same position in 20 years that they find themselves in currently.
309	Rep. Macpherson	Explains his perspective of differences in costs to employees

		and employers in plans.
	Rep. Richardson	Responds that employers pay 14 percent when they pay the pickup and that is tax exempt. States they are not clear on the tax ramifications because they are hoping through the use of the federal code, OARs, and experts the employees can benefit both ways. If the concern is about pre-tax dollars, there is nothing to prevent the employer from paying the six percent into the OSGP, which is tax sheltered for the employee.
334	Rep. Macpherson	Comments that he does not see Rep. Richardson's explanation in the amendments.
	Rep. Richardson	Responds the OSGA is not in the amendments because it already exists.
371	Chair Knopp	Clarifies that Rep. Richardson is saying that instead of the employee putting all of their contribution into the 401A defined contribution, they could put some of theirs into the 457 plan to get the tax deferral.
	Rep. Richardson	Responds that is what he is saying. Adds that there is flexibility in the plan and tax law is not carved in concrete.
388	Rep. Macpherson	Notes the provision for direct review by the Supreme Court in Section 21. Asks what aspects of the Fair Plan raises a concern about whether there would be breach of any contract right.
	Rep. Richardson	Responds that they know of no breach. It is just that this is such an important part of the package that if there should be a challenge they would not want it to be held up any more than any other part of the PERS package.
408	Rep. Macpherson	Compliments Rep. Richardson on his presentation.
416	**Rep. Brown**	**MOTION: Moves to ADOPT HB 2020-6 amendments dated 4/17/03.**
423	Rep. Barker	Asks if it is the Chair's intention to open a work session on HB 2008 today.
	Chair Knopp	Responds he does not plan to and thinks that members will use the HB 2008-1 amendments as the Minority Report on HB 2020.
	Rep. Macpherson	Acknowledges that Chair Knopp is correct.
433		**VOTE: 8-0-1** **EXCUSED: 1 - Rep. Nolan**
	Chair Knopp	**Hearing no objection, declares the motion CARRIED.**
436	**Rep. Brown**	**MOTION: Moves HB 2020 to the floor with a DO PASS AS AMENDED recommendation.**
442	Rep. Barker	Comments that in his opinion a 401K is not a retirement plan, it is a savings plan. If the market goes down, it would be a disaster for the employee who has worked 40 years in public employment and suddenly finds himself without a pension to retire on. States he will vote against this plan because he believes we need to have a piece of stability which is in the hybrid plan.
460	Chair Knopp	Comments that he believes Rep. Barker's statement is accurate to some degree but we are in disaster in a defined benefit plan that we are trying to replace. The difference is who is really responsible in the end. The taxpayers of Oregon are currently responsible for this disaster and the legislature is responsible to find out how to mitigate and work out of the predicament. The HB 2020 plan proposed by Rep. Richardson says this is fair and

		this is what we can afford, and it is certain in terms of what the employer puts in. There is no responsibility for the losses by the taxpayers. The current plan has been great for many public employees but it is only 66 percent funded and he wants to make sure we don't get into this same situation in the future.
TAPE 53, B		
035	Chair Knopp	States that other plans would border on affordable into the future but do start a little bit high and they are not certain. There is a potential without something to keep the costs from escalating to end up at the same place we are, but probably not to the degree we are now. Believes everyone should look at this as a work in progress. It gives the opportunity to advance arguments and move to the Senate.
059	Rep. Barker	Comments that he appreciates the work Rep. Richardson has done on this but is still concerned about future employees getting caught in a down-turned market and not being able to walk out the door. Believes the hybrid plan would resolve that. The problem with the current plan is when they gave out 20 percent instead of eight percent when the actuary said 11 percent, and the legislature did not stop it.
073	Rep. Kafoury	Comments she disagrees with Chair Knopp's assertion that once the employer has paid out their six percent they are through because if the employees end up with no retirement, those employers and the rest of the state are on the hook because the taxpayers will end up paying through food stamps and other services. Also, the assertions that there is stability with this plan because in 20 years things won't change is dreaming because the legislature can change anything at any time. Adds that it is unfortunate that the committee started off having a bi-partisan effort and the plan is being pushed forward without any support from the Democratic members on the committee.
092	Rep. Macpherson	Comments on the working relationship within the committee, and applauds the work by Rep. Richardson. States he will vote against this plan on fundamental philosophy that it is wrong. Thinks we should look after the employees and this plan does not do that. It has a three percent contribution which is all the public employee will get without having to make an individual choice themselves to put money away. That three percent contribution gets accumulated but it must be invested by the member and that member may or may not make good investment decisions. The member has the opportunity to borrow the money; the experience with the loan feature of 401K plans is that a certain portion of the participants borrow against their retirement because they feel they have pressing needs at the time and they don't repay that amount and the account is reduced by the amount that is borrowed. If the employee borrows against the employer contribution, because it is pre-tax, the employee owes tax on the amount of the defaulted loan.
129	Rep. Butler	Comments he thinks some of the views being expressed are short-sighted because of earnings in any period of 10, 20, or 30 years in the market place, with the exception of perhaps those who are looking at the Enron's and others who did not have the ability to invest. States that the legislature cannot legislate good common sense so if someone wanted to go put their investment

		package into a single stock, there is a possibility they could do that. The concern is the long term. Believes that Oregon public employees have a greater propensity to invest in overall instruments in the market place and that indicates the people are becoming more sophisticated. Would hope that when we look at the overall package, we take a look at the entire picture of an employee's useful employable life. Believes the employees will come out in excellent shape and better than plans in the private sector.
152	Chair Knopp	Comments that some have asked about the disability issue. States there is no disability provision in HB 2020. As it relates to disability, believes the legislature needs to act on that, but should act separately, especially as it relates to police and fire.
176		**VOTE: 5-3-1** **AYE: 5 - Brown, Butler, Richardson, Scott, Knopp** **NAY: 3 - Barker, Kafoury, Macpherson** **EXCUSED: 1 - Nolan**
	Chair Knopp	**The motion CARRIES.** **REP. RICHARDSON will lead discussion on the floor.**
183	Rep. Kafoury	Serves notice of a possible Minority Report.
	Chair Knopp	Closes the work sessions on HB 2020 and HB 2003.
	Chair Knopp	Asks if Dave Heynderickx has enough information from the presentation by Margaret Hallock to draft the amendments to HB 2003.
	Dave Heynderickx	Responds he will get the information he needs.
199	Chair Knopp	Comments on the urgency of resolving HB 2003 because it does have budgetary consequences.
202	Chair Knopp	Adjourns the meeting at 4:45 p.m.

EXHIBIT SUMMARY

A – HB 2003, proposal on HB 2003, Margaret Hallock, 6 pp
B – HB 2003, actuarial information, Mark Johnson, 9 pp
C – HB 2020, HB 2020-6 amendments, Rep. Richardson, 59 pp
D – HB 2020, Legislative Fiscal Statement on HB 2020-6 amendments, staff, 3 pp