HOUSE COMMITTEE ON PUBLIC EMPLOYEE RETIREMENT SYSTEM

April 22, 2003 Hearing Room E
3:00 PM Tapes 54 - 55

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. Mary Nolan
Rep. Dennis Richardson
Rep. Wayne Scott

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

MEASURE/ISSUES HEARD: HB 2003 – 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 54, A		
003	Chair Knopp	Calls meeting to order at 3:08 p.m. and opens a work session on HB 2003.
HB 2003 – WORK SESSION		
005	Chair Knopp	Announces that the amendments and fiscal statement for HB 2003 have not been completed. Explains that the key elements of the proposal include the six percent employee contribution and moving that into a transitional account, the eight percent guarantee modification, the two percent cost of living allowance (COLA) issue, elimination of the call, and independent counsel.
016	Greg Hartman	Attorney, PERS Coalition. Summarizes contents of letter relating to contract rights **(EXHIBIT A).** Presents two pages of the Oregon State Police case **(EXHIBIT B).**
098	Hartman	Comments on timelines for passing legislation and suggests the timeline can be changed to allow the legislature time to act. States there is nothing that prevents the PERS Board from delaying any increase for a month or two; it would not have an adverse impact on the system and there is plenty of precedence for that.
114	Hartman	Comments on the Governor's proposal for amendments to HB 2003. The prior version of HB 2003 allowed for a collective bargaining approach to what to do with the six percent employee contribution, and the governor's proposal would have the six percent contributed by employees will be put into a separate account, presumably the equivalent of a defined contribution account. That means the only change being made in PERS is a ratcheting down and eventual elimination of the money match. Does not believe there can be any question that this constitutes an adverse impact on benefits. To the extent the legislature is

		trying to achieve a savings, every dollar of savings is an adverse dollar impact on benefits. The question is whether there is something in the statute which would suggest when the legislature passed the money match that they somehow left the door open to make a change.
160	Hartman	Comments on ORS 238.300, the deletion of the money match, and re-enactment of the money match in 1969 **(EXHIBIT A, page 5).** There is nothing in the statute that indicates they were leaving the door open. Money match is one of the significant benefits of the plan. If we apply the analysis of the courts, this proposal will have a great deal of difficulty getting by the Supreme Court.
183	Hartman	The second part goes to the eight percent guarantee. They feel the Governor's office has re-analyzed ORS 238.255 and has come to the conclusion it was the intention of the legislature in the early 1970s to guarantee that each employee would receive over the course of their career eight percent or the guaranteed rate and not on a yearly basis. Quotes language shown on page 6 **(EXHBIIT A).** The language is very promissory in nature. Takes exception with the Governor's analysis. If we set aside the interpretation, we are back to where we were with the Measure 8 case. This proposal would do away with the guarantee. Assumes if this passes, there will not be a required payment for most if not all of Tier I participants throughout the remainder of their careers. That is the equivalent of eliminating the guarantee and it is what the court has said you cannot do. There is no difference between this proposal and Measure 8 unless you can support the Governor's reading of the statute that this is not meant to be yearly. The statute says this is something that is going to happen each year.
248	Hartman	Also in the Governor's proposal eliminates cost of living allowance (COLA) increases for a targeted group of retirees. Those who retired after 1999 and before 2004 are not going to receive COLA payments until there has been some payback. This proposal is no better than Judge Lipscomb's opinion, and with all respect to Judge Lipscomb we will not know how good his opinion is until it is reviewed in the higher courts. Judge Lipscomb made the decision on behalf of eight employers and if the legislature moves on the proposal that would be treating it as if Judge Lipscomb made the decision for all employers One has to look at the language regarding the COLA. It is promissory and says a benefit will be paid to retirees. The proposal flies in the face of some very specific promissory language.
288	Hartman	Thinks the proposal is too far a simplistic approach. If you go too far, the courts may say it is impairment. But if the court rules in our favor there is much more likely to be a breach of contract than an impairment of contract.
	Hartman	It could be, if there is a decision that the legislative enactment has breached the contract, individual employers and the state will be liable for those damages. It is not a circumstance for a free pass to see how it works out.
357	Hartman	States that that he finds no unifying concept in the governor's proposal which redefines what pension contract rights will mean henceforth, assuming the Supreme Court says this is fine. Asks

		what value will the PERS promise have in the future if this legislature can enact this proposal and the next legislature can chip more off. You will have a system but not one that is viewed favorably by employees or employers. Unless there is some unifying concept which redefines what a pension contract means in Oregon, it doesn't mean much of anything. If you want to adopt the governor's proposal, it is a tremendous risk. States he is most troubled that there are no unifying principles in the proposal that says what a pension contract promise in Oregon will mean two or three or four years from now.
408	Chair Knopp	Comments that the assumed rate is over a large period of time. Asks if there is an assumed rate over 26 years but a guarantee that is examined each year, why would the court not say there is an eight percent guarantee but the contract is longer than each year, and it assumes eight percent would be paid in the years when there is are eight percent earnings, it would be legitimate to modify that and pay it off over a longer period of time.
437	Hartman	Respond that when the legislature passed this in the early 1970s there was no reserve account. There had been two years of zero earnings which lead up to the effort to pass the statue. The account referenced was a deficit account. Over the many years since then, the reserve has been sufficient. The legislature did not say in 1973 that there would be a guaranteed rate if there is a reserve to pay it from. The courts start with reading the language of the statute and say if the language of the statute is clear, they don't have to look at much of anything else. Thinks the statute is very clear that it contemplates a yearly allocation of the guaranteed rate. The statute has been held to be part of the pension contract. Does not think the legislature can get to the position of having this sustained either by the governor finding meaning, which he does not believe is here, and doesn't think one can get there by saying we made the promise but don't have the account and therefore should not have to follow the promise. Believes the court will have great difficulty with that approach.
TAPE 55, A		
034	Chair Knopp	Comments if there is an eight percent guarantee and it is built on a 26-year range, if you credit more than eight percent in any given year, you will never be able to fund the eight percent guarantee unless you have earnings beyond that. It seem illogical that the courts would not look at that and say it was flawed from the outset in terms of the crediting policy and needs to be fixed.
	Hartman	Responds that the courts have never been willing to say that simply because the legislature may have made an error in judgment that the court will bail them out and save them. Over the last several years there have been instances where the legislature has acted and the courts have said very specifically that if the legislature does it and it is clear that the legislature did it, and in hindsight it may not have been the best idea, we won't bail them out. Thinks this is very much what we have here.
061	Chair Knopp	Comments that regardless of whether the legislature agrees with the 1973 legislature and the eight percent guarantee, the legislature did not credit beyond eight percent, the PERS Board did that, and is part of the case that Judge Lipscomb ruled on in

		terms of excess crediting. It seems illogical that that would not be taken into account as it relates to the guarantee if they are going to uphold Lipscomb.
	Hartman	States that he thinks the court operates under a set of rules when they act on legislative enactments. They recognize the legislature is the policy maker.
078	Rep. Richardson	Comments on historical, legal, and social aspects in the history of Oregon PERS. States that in the Hughes case one of the footnotes refers to a 1953 attorney general opinion on whether adjustments can be made in retirement plans. The opinion stated that the ruling permitting modification of pensions is a necessary one since pensions systems must be kept flexible to permit adjustments in accord with changing conditions, and at the same time maintain the integrity of the system and carry out its beneficial policy. There was a change in the retirement plan in the 1950s. Historically, does not believe that Hartman's position is necessarily fully sustained.
101	Rep. Richardson	Notes that Hartman has given a lot of weight in his letter to unilateral contracts and the fact that when a contract is made one person cannot change it. It seems the parameter of the argument is based on a situation where both sides enter into a contract and they both know what is to be expected from each other, and there is an expectation that both sides will be able to perform so one side backs off. Wonders if another contractual legalism of mutual mistake may not apply here since what is being proposed in HB 2003 is not a termination of the PERS contract, but a reinterpretation of the allocation of benefits from the way the PERS Board chose to allocate them in the late 1990s and in doing it not deprive members of benefits but allocate those benefits not all at once and take what you get in down markets but allocate with the understanding or premise that the eight percent accrued interest benefit was an average that was anticipated for 40 years and not a floor that the employee was going to get no matter what and anything above it. It seems there are other ways that could be looked at.
121	Rep. Richardson	States that the third part is the social aspect because as the pension plan was originally implemented and accepted by the employees it was in anticipation of a benefit that was somewhere in the range of 50-70 percent and neither side anticipated that a strange alignment of events would result in pension benefits that are averaging over 100 percent and will be averaging nearly 125 percent and 200 percent of their best wages. That windfall has the unanticipated consequence of affecting all aspects of our society.
144	Rep. Richardson	States he is grateful for the legal approach and the quotes from Hartman. Thinks there will be more at stake than merely one legal approach to it as compared to another equally valid legal approach—meaning this has been a mutual mistake. What we have is a change in benefits, not a termination of benefits.
148	Hartman	Asks what pension protection individual members would have if Rep. Richardson's approach is adopted by the courts.
250	Chair Knopp	Notes that the committee has letters from Kenneth Daughton **(EXHBIIT C)** and Catherine Bloom, Eugene Water & Electric Board **(EXHIBIT D).**

230	Bill Gary	Attorney. Explains the goals of his clients when they asked to have HB 2003 introduced. They sought to reduce the escalating cost of the retirement system and to try to begin to bring under control the unfunded actuarial liability. They sought to remedy the effects of past unlawful actions taken by the PERS Board, to some extent identified in the *City of Eugene* decision by Judge Lipscomb.
305	Gary	Comments on increasing cost of the system, including money match, the eight percent guarantee that has driven costs and the practices of the PERS Board that have the effect of increasing benefits. Believes HB 2003 accomplishes both goals and do so in a way calculated as best as human ability permits. States that while it may be prudent to take no action if the risk associated with the action is great, it is not prudent to do nothing if the risks of taking no action are demonstrably greater.
342	Gary	States that the amendments that were proposed, subject to details, are a constructive example of how to improve a proposal. Believes they are on the verge of a far reaching and a fairer solution than the initial proposal.
356	Gary	States it is important that the bill address the three main areas identified by Judge Lipscomb and provide remedies for those actions. It is important to provide remedies for all three; they are different. Two things identified that affect only people who have retired—the calculation of the money match benefit for people participating in the variable account, and the calculation of benefits using outdated mortality tables. People who have not retired are not affected by those unlawful actions because those actions take place at retirement.
374	Gary	States the third problem identified is over crediting, the crediting to member accounts imprudent amounts in good years and leaving inadequate reserves to cover the down years. While Hartman is correct that the lawsuit was brought on behalf of eight employers, the eight employers challenged a decision in 2000 that allocated investment income to every single account in the PERS fund. After a trial, Judge Lipscomb said the employers were correct, and the PERS Board was incorrect in the way they allocated income and ordered the Board to go back and do it again. States that Hartman is simply wrong when he says the decision only affects the eight employers as a matter fact and as a matter of law. As to the 1999 earnings, that is a decision by the Circuit Court that requires the PERS Board to go back and reallocate those earnings for every account, not the accounts of the eight employers.
402	Gary	States the proposed amendment deals with the problem of over crediting and believes it is a creative and more fair way than the original bill because it will ensure that everyone who was a member of Tier I PERS when they retire will have an account balance that is at least equal to the accumulated contributions plus interest credited on that account at the assumed rate. In all likelihood many members will still retire with far more than that. The amount that has been credited in excess of the assumed rate will be available in a reserve account to even out the investment crediting in the down years. This bill provides a mechanism to recoup the excessive crediting in a way that does

		not require the board to go in and immediately alter the account balances of members and take money out of the accounts.
437	Gary	Refutes position of Hartman that the language says the accounts must be credited each year and the issue of contract rights. Comments on *PGE vs. Bureau of Labor and Industries.* The issue is not what the statute means, but what is the content of the statutory contractual promise, if any, that was made. They were guaranteed that they would be credited with no less than eight percent, not that they would get eight percent in the down years and 20 percent in the good years. Believes their coalition is not in opposition to the bill previously passed that capped the crediting of the assumed rate at the assumed rate so that Tier I accounts would not receive more than the assumed rate, at least until certain conditions are met.
TAPE 54, B		
018	Gary	Comments on comment by Hartman that the money match language is specifically promissory in nature. States he is not sure what that means. The court has never said that the way you determine whether something is a contractual promise or not is by looking at whether the language is specifically promissory in nature. The court has said you look at what the legislature intended. States he has never heard Hartman dispute the fact that when the money match language was included in the statute, it was included to protect a very limited number of existing members in 1969 and not to be one of the most important benefits that is provided to PERS members.
030	Gary	Believes the amendments are on the right track. Looks forward to the amendments being printed and will offer full support when they are.
041	Rep. Nolan	Asks when the Eugene case was filed.
	Gary	Explains that some clients filed in 1999 and some did not file until 2000. Three orders are being challenged: the 1999 earnings allocation, the 1998 rate orders, and the 2000 rate orders. Not all the petitioning employers challenged all the orders.
053	Rep. Nolan	Comments that the challenge has been principally to 1999, and now Gary references 1998.
	Gary	Responds they only challenged the 1999 earnings allocation. There was no challenge filed to prior year's earnings allocations.
066	Rep. Nolan	Asks why they didn't notice the first time earnings were credited above eight percent.
087	Gary	States he believes in 1998 there was a dramatic increase in employer contribution rates for many participating employers and that was a wake up call for many. Believes they assumed the robust earnings were producing a wonderful situation for everyone, and it wasn't until their rates increased in a year when the fund had wonderful earnings that they began asking why they were being asked to pay more to support the system.
114	Rep. Nolan	Comments she believes the system should be solvent for everyone involved. Asks if his clients brought legislation in 1999 to cap earnings credits.
	Gary	States that since he has been involved employers have been in the legislature asking for reforms that would curb the rising costs.
138	Rep. Nolan	Comments that the legislature, without passing judgment, did not

		see merit in the proposals to take action. Asks if it would be fair to assume the legislature was essentially saying that the policy on the books was the policy it wanted to have on the books.
	Gary	Comments he cannot draw any inference for legislative inaction. Two years ago there were amendments to the reserving statutes that intended to address the problem. However, they had not diagnosed the problem they were trying to solve so it didn't get at the problem. It wasn't that the legislature was turning a blind eye to the problem, but it did not get the attention it is receiving in this session.
164	Rep. Nolan	Comments there was nothing to prevent the 1999, 1979, or 2001 legislature from saying they want to make sure people understand that the legislature thinks of the assumed interest rate as not just a floor but a ceiling as well.
184	Chair Knopp	Closes the work session on HB 2003 and adjourns meeting at 4:17 p.m.

EXHIBIT SUMMARY

A – HB 2003, letter, Greg Hartman, 7 pp
B – HB 2003, pages from court case, Greg Hartman, 1 p
C – HB 2003, written testimony, Kenneth Daughton, 2 pp
D – HB 2003, letter, Catherine Bloom, 8 pp