Agenda

ND Teachers' Fund for Retirement Board Meeting

Thursday, May 16, 2013
1: 00 pm

Peace Garden Room, State Capitol
Bismarck, ND

1. Call to Order and Approval of Agenda - Pres. Gessner
2. Approval of Minutes of March 21, 2013 Meeting – Pres. Gessner
3. 2013 Legislative Wrap Up – Fay Kopp
4. 2011 Legislative Implementation Update – Shelly Schumacher
5. Board Education: TFFR Board Responsibilities – Fay Kopp
6. Dep Exec Director/Chief Retirement Officer position – Jan Murtha
7. Board Resolutions for Bob Toso and Lowell Latimer – Pres. Gessner

~~ RETIREMENT COFFEE PARTY honoring Bob Toso and Lowell Latimer ~~

8. Annual Technology Review – Gary Vetter
9. SIB Update – Darren Schulz
10. SIB Search Committee Update – Treas. Schmidt, Pres. Gessner
11. TFFR Centennial Celebration – Fay Kopp
12. 2013-14 Board Calendar and Education Plan – Fay Kopp
13. Consent Agenda
14. Other Business
15. Adjournment

Next Board Meeting: July 25, 2013

Any person who requires an auxiliary aid or service should contact the Retirement and Investment Office at 701-328-9885 at least three (3) days before the scheduled meeting.

NORTH DAKOTA TEACHERS' FUND FOR RETIREMENT
MINUTES OF THE
MARCH 21, 2013, BOARD MEETING

BOARD MEMBERS PRESENT:	Mike Gessner, President Kirsten Baesler, State Superintendent Clarence Corneil, Trustee Kim Franz, Trustee Lowell Latimer, Vice President Kelly Schmidt, State Treasurer Bob Toso, Trustee
STAFF PRESENT:	Fay Kopp, Interim Executive Director Darlene Roppel, Retirement Assistant Darren Schulz, Interim CIO Shelly Schumacher, Retirement Program Manager
OTHERS PRESENT:	Rolland Larson, NDRTA Janilyn Murtha, Attorney General's Office Kim Nicholl, Segal Company (teleconference) Matt Strom, Segal Company (teleconference)

CALL TO ORDER:

Mr. Mike Gessner, President of the Teachers' Fund for Retirement (TFFR) Board of Trustees, called the board meeting to order at 1:00 p.m. on Thursday, March 21, 2013, at the Workforce Safety & Insurance Office (WSI), 1600 E Century Avenue, Bismarck, ND.

THE FOLLOWING MEMBERS WERE PRESENT REPRESENTING A QUORUM: PRESIDENT GESSNER, SUPT. BAESLER, MR. CORNEIL, MRS. FRANZ, DR. LATIMER, TREASURER SCHMIDT, AND MR. TOSO.

APPROVAL OF AGENDA:

The Board considered the meeting agenda. President Gessner requested discussion of the Deputy Executive Director's position be added to Agenda Item 7.

MR. TOSO MOVED AND MRS. FRANZ SECONDED TO APPROVE THE AGENDA WITH THE ADDITION.

AYES: MR. CORNEIL, TREASURER SCHMIDT, SUPT. BAESLER, MR. TOSO, MRS. FRANZ, DR. LATIMER, AND PRESIDENT GESSNER.
NAYS: NONE
MOTION CARRIED.

MINUTES:

The Board considered the minutes of the regular board meeting held January 24, 2013.

DR. LATIMER MOVED AND MR. CORNEIL SECONDED TO APPROVE THE MINUTES OF THE REGULAR TFFR BOARD MEETING HELD JANUARY 24, 2013, AS PRESENTED.

AYES: MR. TOSO, DR. LATIMER, TREASURER SCHMIDT, MR. CORNEIL, SUPT. BAESLER, MRS. FRANZ, AND PRESIDENT GESSNER.
NAYS: NONE
MOTION CARRIED.

TFFR FUNDING POLICY:

Ms. Kim Nicholl and Mr. Matt Strom, Segal Company, joined the meeting by teleconference, to review the Statement of Actuarial Funding Policy drafted by Segal Company and staff. This statement incorporates Segal's recommendations approved at the January 2013, TFFR board meeting: entry age normal cost method based on traditional method, actuarial assets based on 5-year smoothing with an 80%/120% corridor, and amortization period of 30-year closed with flexibility to manage the volatility as deemed appropriate. This funding policy complies with the Government Finance Officers Association (GFOA) best practices for development of funding policies.

After discussion,

MR. CORNEIL MOVED AND MR. TOSO SECONDED TO APPROVE THE FUNDING POLICY TO BE EFFECTIVE FOR THE JULY 1, 2013, ACTUARIAL VALUATION.

AYES: TREASURER SCHMIDT, SUPT. BAESLER, MR. CORNEIL, MRS. FRANZ, DR. LATIMER, MR. TOSO, AND PRESIDENT GESSNER.
NAYS: NONE
MOTION CARRIED.

ACTUARIAL CONTRACT:

Mrs. Fay Kopp, Interim Executive Director, reviewed a proposal dated March 5, 2013, from Segal Company to extend their actuarial consulting contract with TFFR for the two year period from July 1, 2013 – June 30, 2015. Mrs. Kopp distributed a graph showing actuarial consulting fees paid from 2003 – 2012. She explained that actuarial costs are largely impacted by legislative proposals, special studies, compliance issues, and board initiatives.

After board questions and discussion,

TREASURER SCHMIDT MOVED AND MR. TOSO SECONDED TO EXTEND THE CONTRACT WITH SEGAL COMPANY FOR THE 2013-2015 YEARS.

AYES: MRS. FRANZ, MR. CORNEIL, MR. TOSO, DR. LATIMER, TREASURER SCHMIDT, SUPT. BAESLER, AND PRESIDENT GESSNER.
NAYS: NONE
MOTION CARRIED.

LEGISLATIVE UPDATE:

Mrs. Kopp gave an update on 2013 legislative issues.

HB 1022, the Retirement and Investment Office (RIO) budget, had a hearing on March 14, 2013, in the Senate Appropriations Committee. No action has been taken.

HB 1230, which maintains TFFR member and employer contribution rates approved by the 2011 Legislature until the fund reaches 100% funded ratio rather than 90%, has been approved and sent to the Governor for signature.

HB 1304, divestiture of state investment funds, had a hearing earlier in March at which Mr. Darren Schulz, Interim CIO, Mrs. Kopp and Treasurer Schmidt, representing their individual organizations, each testified against the bill. No committee action has been taken at this time.

HCR 3003, state retirement stabilization fund, could affect TFFR in the future. If passed, it will be on the ballot in 2014. Mrs. Kopp will continue to monitor.

SB 2059, PERS funding recovery, is being monitored. It has been amended in the House to include an interim study of state retirement plans, which could include TFFR. The Committee has not taken any action.

SB 2061, TFFR administrative changes, was passed and signed by the Governor.

SIB UPDATE:

Mr. Schulz reported there have been many positive developments in the investment environment. The estimated total investment return fiscal year to March 20, 2013, is about 12% for TFFR.

Mr. Schulz reviewed the agenda for the SIB meeting to be held March 22, 2013. Mr. Schulz provided information on the Bank of North Dakota and watch list discussion.

SIB SEARCH COMMITTEE UPDATE:

Treasurer Schmidt and Mr. Toso updated the board on the progress in hiring the SIB Executive Director/Chief Investment Officer. Two hundred applications were received. The top 30 were reviewed by Treasurer Schmidt, Mr. Schulz, Mrs. Connie Flanagan, Fiscal and Investment Officer, and Mr. Mike Sandal, PERS board. The Search Committee decided that it was necessary to expand the search and enlist the services of an executive recruitment service. A Request for Proposal (RFP) has been issued.

Mr. Toso informed the Board he will be resigning from the Search Committee after the search firm is hired due to his retirement. President Gessner volunteered to replace him.

There was some board discussion on TFFR's role or possible future input in the evaluation and hiring of the Deputy Executive Director – Chief Retirement Officer position. This will be placed on the agenda of the May 16, 2013, meeting for further discussion and information to be provided by Mrs. Kopp.

The board recessed at 2:50 p.m. and reconvened at 3:00 p.m.

TFFR CENTENNIAL:

TFFR is 100 years old this year. There was discussion on ways of observing this occasion. Mrs. Kopp will discuss with the North Dakota Education Association (NDEA), North Dakota Council of Educational Leaders (NDCEL) and North Dakota Retired Teachers Association (NDRTA) and bring information back to the May 2013, meeting.

2013-14 BOARD MEETING SCHEDULE:

Mrs. Kopp reviewed the proposed 2013-14 TFFR-SIB meeting schedule. The Board agreed to schedule an April 24, 2014, meeting and no meeting in May 2014, unless it is necessary. Mrs. Kopp will bring the 2013-14 board calendar and education plan back to the May 2013, meeting for approval.

The next regular TFFR board meeting will be held May 16, 2013.

CONSENT AGENDA:

MR. TOSO MOVED AND MRS. FRANZ SECONDED TO APPROVE THE CONSENT AGENDA WHICH INCLUDES TWO DISABILITY APPLICATIONS – 2013-4D AND 2013-5D.

AYES: DR. LATIMER, MR. TOSO, MRS. FRANZ, SUPT. BAESLER, MR. CORNEIL, TREASURER SCHMIDT, AND PRESIDENT GESSNER.
NAYS: NONE
MOTION CARRIED.

OTHER BUSINESS:

Mrs. Kopp referenced the presentation that was given at the North Dakota School Board Association (NDSBA) Negotiations Seminar by Mrs. Kopp and Mrs. Shelly Schumacher, Retirement Program Manager.

ADJOURNMENT:

With no further business to come before the Board, President Gessner adjourned the meeting at 3:35 p.m.

Respectfully Submitted:

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Mr. Mike Gessner, President
Teachers' Fund for Retirement Board

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Darlene Roppel
Reporting Secretary

MEMORANDUM

TO: TFFR Board

FROM: Fay Kopp

DATE: May 9, 2013

SUBJ: 2013 LEGISLATIVE WRAP UP

Here is a brief recap of some of the 2013 legislative proposals affecting TFFR.

BILLS THAT FAILED

- HB 1203, Retiree re-employment (Rep. Drovdal)
  Would have removed the requirement for TFFR member contributions to be paid on salary earned by re-employed retirees.

- HB 1304, Iran divestiture (Rep. Grande)
  Would have required certain restrictions, monitoring, and reporting of scrutinized companies under Iran Sanctions Act, within SIB portfolios.

- SB 2150, Board member compensation (Sen. Andrist)
  Would have restricted per diem compensation for board members to that of legislative pay, and disallowed a governmental employee from receiving both compensation for the employment and per diem compensation for service as a board member for same day of service.

- SB 2331, Retiree-re-employment (Sen. Heckaman)
  Would have required a re-employed retiree's benefit to be actuarially adjusted to provide an increase based on the total amount of member contributions paid during re-employment.

- HCR 3003, State Retirement Stabilization Fund (Rep. Delzer)
  Would have added 2 new sections to the ND Constitution to be voted on in the 2014 general election. Would have limited growth of foundation aid stabilization fund and transferred excess oil revenues to a new state retirement stabilization fund which would be used to address unfunded retirement benefit obligations of a state retirement system.

- SCR 4010, Oil Taxes – State Retirement Stabilization Fund (Sen. Hogue)
  As amended, would have done same as HCR3003 (above) and created a new state retirement stabilization fund with excess oil revenues which would be used to address unfunded retirement benefit obligations of a state retirement system.

BILLS THAT PASSED

- HB 1022, RIO Budget (Governor's Office)
  Approved as submitted. Legislature added state employee salary and benefit package changes, and 1 new FTE for an Investment Analyst for SIB program.

- HB 1230, Reduce TFFR contributions at 100% funded level (Rep. Louser)
  Approved as submitted. Member and employer contributions will be reduced to 7.75% each when TFFR reaches 100% funded level.

- HB 1452, PERS DC option for new employees, PERS funding improvement, and state retirement plan study (Rep. Kasper), summarized below:

  Optional DC election for new state employees effective 1/1/14. Provision will sunset in 2017.

  PERS 1% contribution increase effective 1/1/14 for State and employees (total 2%). Contribution rates will be reduced once PERS plan reaches 100% funded level. 2015 contribution increases were removed.

  Interim Legislative Management study of state retirement plans. Study must include an analysis of both DB and DC plan with considerations and consequences for transitioning to a state DC plan. Study may not be conducted by legislative employee benefits programs committee.

- SB 2061, TFFR technical changes (TFFR Board)
  Approved as submitted. No financial impact on TFFR plan.

MEMORANDUM

TO: TFFR Board

FROM: Shelly Schumacher

DATE: May 16, 2013

SUBJ: 2011 Legislative Implementation Update

Since your last update in July 2012, TFFR staff continues to make progress on implementing the 2011 legislative changes. We are on schedule to complete the implementation prior to the effective dates of the changes noted below.

HB 1133	Administrative changes	08-01-11
HB 1134	Contribution increases	07-01-12
	Benefit changes	07-01-13
	Contribution increases	07-01-14

<u>Communications</u>

- TFFR Newsletters
  Employer Newsletter (quarterly)
  Active Member Newsletter (semi-annual)
  Retired Member Newsletter (semi-annual)

- Annual Statement (non-retired)
  Removed benefit projections from the annual statements and included letter outlining impact of legislation in August 2011, 2012 and 2013. The August 2013 annual statement will show the member's new Tier (Tier 1 Grandfathered, Tier 1 Non-grandfathered, or Tier 2). The August 2014 annual statements will again show benefit projections based on the new Tier.

- RIO – TFFR website
  Post presentations, legislative information, publications, etc.

- Interest Group Conferences
  NDSBMA Spring Workshops
  NDRTA Annual Conference
  NDEA Annual Conference
  NDCEL Annual Conference
  NDSBA Annual Conference
  Other Meetings and Conferences by Request

- TFFR Preretirement Seminars

- TFFR Benefits Counseling Sessions

Publications and Forms

Updated Employer Guide, Member Handbook, brochures
Updated all member and employer forms and form letters

System programming modifications

HB 1133 – system programming complete

HB 1134 –

- Phase 1 - contribution increases

  Employer reporting / retiree re-employment / employer payment plan model changes / purchase of service

  Build 1: Contribution increases to employer reporting and change to tax methodology for partial employer payment models programmed and tested – *in production*

  Build 2: Changes to retiree re-employment – *in production*

  Build 3: Update to purchase of service cost calculation programmed and tested – *in production*

CPAS cost for Phase 1 of HB1134 - $59,910

- Phase 2 - benefit changes (estimated completion date – June 2013)

  Grandfathering determination / retirement calculation / disability calculation / purchase of service

  Build 1: Grandfathering calculation – *tested and ready for production*

  Build 2 – Changes to retirement eligibility, early retirement reduction factor, and disability eligibility and benefit calculation – *tested and ready for production*

  Build 3 – Changes to Year End calculation used to create valuation files and annual statements – *tested and ready for production*

  Build 4 – Update purchase of service cost calculation – *TFFR testing update delivered on May 2*

  TFFR staff plans to modify all of the reports, statements, and letters that are impacted by the legislative changes – *95% complete*

CPAS estimated cost for Phase 2 of HB1134 - $102,080

MEMORANDUM

TO: TFFR Board

FROM: Fay Kopp

DATE: May 9, 2013

SUBJ: BOARD EDUCATION: TFFR Board Responsibilities

Enclosed are copies of state statutes outlining TFFR, SIB, and RIO authority as it relates to the TFFR retirement program. At the May board meeting, I plan to make a brief presentation describing TFFR Board responsibilities.

In addition, Jan Murtha, TFFR legal counsel, has reviewed board statutory authority, and will be available to make some comments on this topic.

Enclosures

CHAPTER 54-52.5
STATE RETIREMENT AND INVESTMENT OFFICE

54-52.5-01. North Dakota state retirement and investment office.

The state retirement and investment office is created to coordinate the activities of the state investment board and teachers' fund for retirement.

54-52.5-02. Governing authority.

The state investment board shall govern the state retirement and investment office. The state investment board is responsible for overseeing and operating the agency and may do all things necessary to coordinate the activities of the state investment board and the teachers' fund for retirement. The board of trustees of the teachers' fund for retirement and the state investment board shall maintain their legal identities and authority as otherwise provided by law.

54-52.5-03. State retirement and investment fund - Cost of operation of agency.

A special fund known as the "state retirement and investment fund" is established for the purpose of defraying administrative expenses of the state retirement and investment office. The actual amount of administrative expenses incurred by the state retirement and investment office must be paid from the respective funds listed under section 21-10-06 and are hereby appropriated to the state retirement and investment fund in proportion to the services rendered for each fund as estimated by the state investment board. The amount necessary to pay all administrative expenses of the state retirement and investment office must be paid from the state retirement and investment fund in accordance with the agency's appropriation authority. Any interest income earned on the state retirement and investment fund must be credited to the fund.

15. "Tier two member" means a teacher who is not a tier one member.

15-39.1-05. Management of fund.
Repealed by S.L. 1997, ch. 170, § 4.

15-39.1-05.1. Board composition - Terms - Voting.
1. The authority to set policy for the fund rests in a board of trustees composed as follows:
   a. The governor shall appoint, from a list of three nominees submitted to the governor by the North Dakota education association, two board members who are actively employed in full-time positions not classified as school administrators. A board member appointed under this subdivision who terminates employment may not continue to serve as a member of the board.
   b. The governor shall appoint, from a list of three nominees submitted to the governor by the North Dakota council of educational leaders, one board member who is actively employed as a full-time school administrator. A board member appointed under this subdivision who terminates employment may not continue to serve as a member of the board.
   c. The governor shall appoint, from a list of three nominees submitted to the governor by the North Dakota retired teachers association, two board members who are the retired members of the fund.
   d. The state treasurer and the superintendent of public instruction.
2. All current appointees of the board shall serve the remainder of their terms as members of the board until their terms expire and their successors are appointed. The first newly appointed board member under subdivision a of subsection 1 must be appointed to serve an initial term of four years. The first newly appointed board member under subdivision c of subsection 1 must be elected to serve an initial term of five years. Newly appointed board members shall serve a term of five years. Each newly appointed term begins on July first.
3. Each board member is entitled to one vote, and four members constitute a quorum. Four votes are required for resolution or action by the board.

15-39.1-05.2. Board authority - Continuing appropriation.
The board:
1. Has the powers and privileges of a corporation, including the right to sue and be sued in its own name. The venue of all actions to which the board is a party must be Burleigh County.
2. Shall establish investment policy for the trust fund under section 21-10-02.1. The investment policy must include:
   a. Acceptable rates of return, liquidity, and levels of risk; and
   b. Long-range asset allocation targets.
3. Shall arrange for actuarial and medical consultants. The board shall cause a qualified, competent actuary to be retained on a consulting basis. The actuary shall:
   a. Make a valuation of the liabilities and reserves of the fund and a determination of the contributions required by the fund to discharge its liabilities and pay administrative costs;
   b. Recommend to the board rates of employer and employee contributions required, based upon the entry age normal cost or other accepted actuarial method, to maintain the fund on an actuarial reserve basis;
   c. Once every five years make a general investigation of the actuarial experience under the fund, including mortality, retirement, employment turnover, and other items required by the board;
   d. Recommend actuarial tables for use in valuations and in calculating actuarial equivalent values based on the investigation provided for in subdivision c; and
   e. Perform other duties assigned by the board.

4. May pay benefits and consultant fees as necessary which are hereby appropriated from the fund.
5. Shall submit to the legislative management's employee benefits programs committee any necessary or desirable changes in statutes relating to the administration of the fund.
6. Shall determine appropriate levels of service to be provided to members, including benefits counseling and preretirement programs.
7. Shall, through resolution, inform the state investment board, which is the administrative board of the retirement and investment office, the levels of services, goals, and objectives expected to be provided through the retirement and investment office.

15-39.1-06. Organization of board.

The board may hold meetings as necessary for the transaction of business and a meeting may be called by the president or any two members of the board upon reasonable notice to the other members of the board. The president for the ensuing year must be elected at the first meeting following July first of each year.

15-39.1-07. Vacancies - Rulemaking power.

Vacancies which may occur among the appointed members of the board must be filled by the governor and the appointee shall complete the term for which the original member was selected. The board may adopt such rules as may be necessary to fulfill the responsibilities of the board.

15-39.1-08. Compensation of members.

Members of the board, excluding ex officio members, are entitled to receive one hundred forty-eight dollars as compensation per day and necessary mileage and travel expenses as provided in sections 44-08-04 and 54-06-09 for attending meetings of the board. No member of the board may lose regular salary, vacation pay, vacation or any personal leave, or be denied right of attendance by the state or political subdivision thereof while serving on official business of the fund.

15-39.1-09. (Contingent expiration date - See note) Membership in fund and assessments - Employer payment of employee contribution.

1. Except as otherwise provided by law, every teacher is a member of the fund and must be assessed upon the teacher's salary seven and seventy-five hundredths percent per annum, which must be deducted, certified, and paid monthly to the fund by the disbursing official of the governmental body by which the teacher is employed. Member contributions increase to nine and seventy-five hundredths percent per annum beginning July 1, 2012, and increase thereafter to eleven and seventy-five hundredths percent per annum beginning July 1, 2014. Except as otherwise provided by law, every governmental body employing a teacher shall pay to the fund eight and seventy-five hundredths percent per annum of the salary of each teacher employed by it. Contributions to be paid by a governmental body employing a teacher increase to ten and seventy-five hundredths percent per annum beginning July 1, 2012, and increase thereafter to twelve and seventy-five hundredths percent per annum beginning July 1, 2014. The required amount of member and employer contributions must be reduced to seven and seventy-five hundredths percent per annum effective on the July first that follows the first valuation showing a ratio of the actuarial value of assets to the actuarial accrued liability of the teachers' fund for retirement that is equal to or greater than ninety percent. The disbursing official of the governmental body shall certify the governmental body payments and remit the payments monthly to the fund.
2. Each employer, at its option, may pay the teacher contributions required by subsection 1 for all compensation earned after June 30, 1983. The amount paid must be paid by the employer in lieu of contributions by the employee. If an employer

CHAPTER 21-10
STATE INVESTMENT BOARD

21-10-01. State investment board - Membership - Term - Compensation - Advisory council.

1. The North Dakota state investment board consists of the governor, the state treasurer, the commissioner of university and school lands, the director of workforce safety and insurance, the insurance commissioner, three members of the teachers' fund for retirement board or the board's designees who need not be members of the fund as selected by that board, two of the elected members of the public employees retirement system board as selected by that board, and one member of the public employees retirement system board as selected by that board. The director of workforce safety and insurance may appoint a designee, subject to approval by the workforce safety and insurance board of directors, to attend the meetings, participate, and vote when the director is unable to attend. The teachers' fund for retirement board may appoint an alternate designee with full voting privileges to attend meetings of the state investment board when a selected member is unable to attend. The public employees retirement system board may appoint an alternate designee with full voting privileges from the public employees retirement system board to attend meetings of the state investment board when a selected member is unable to attend. The members of the state investment board, except elected and appointed officials and the director of workforce safety and insurance or the director's designee, are entitled to receive as compensation one hundred forty-eight dollars per day and necessary mileage and travel expenses as provided in sections 44-08-04 and 54-06-09 for attending meetings of the state investment board.
2. The state investment board may establish an advisory council composed of individuals who are experienced and knowledgeable in the field of investments. The state investment board shall determine the responsibilities of the advisory council. Members of the advisory council are entitled to receive the same compensation as provided the members of the advisory board of the Bank of North Dakota and necessary mileage and travel expenses as provided in sections 44-08-04 and 54-06-09.

21-10-02. Board - Powers and duties.

The board is charged with the investment of the funds enumerated in section 21-10-06. It shall approve general types of securities for investment by these funds and set policies and procedures regulating securities transactions on behalf of the various funds. Representatives of the funds enumerated in section 21-10-06 may make recommendations to the board in regard to investments. The board or its designated agents must be custodian of securities purchased on behalf of funds under the management of the board. The board may appoint an investment director or advisory service, or both, who must be experienced in, and hold considerable knowledge of, the field of investments. The investment director or advisory service shall serve at the pleasure of the board. The investment director or advisory service may be an individual, corporation, limited liability company, partnership, or any legal entity which meets the qualifications established herein. The board may authorize the investment director to lend securities held by the funds. These securities must be collateralized as directed by the board. The board may create investment fund pools in which the funds identified in section 21-10-06 may invest.

21-10-02.1. Board - Policies on investment goals and objectives and asset allocation.

1. The governing body of each fund enumerated in section 21-10-06 shall establish policies on investment goals and objectives and asset allocation for each respective fund. The policies must provide for:
   a. The definition and assignment of duties and responsibilities to advisory services and persons employed by the board.
   b. Acceptable rates of return, liquidity, and levels of risk.

c. Long-range asset allocation goals.
d. Guidelines for the selection and redemption of investments.
e. Investment diversification, investment quality, qualification of advisory services, and amounts to be invested by advisory services.
f. The type of reports and procedures to be used in evaluating performance.
2. The asset allocation for each fund, to be effective, must be approved by the governing body of that fund and the state investment board by January first of each year. If the asset allocation is not approved, the previous asset allocation remains effective. The governing body of each fund shall use the staff and consultants of the retirement and investment office in developing asset allocation and investment policies.

21-10-03. Cooperation with Bank of North Dakota.
Repealed by S.L. 1987, ch. 190, § 14.

21-10-04. Board - Meetings.
The state investment board shall select one of its members to serve as chair, one to serve as vice chair, and shall meet at the call of the chair or upon written notice signed by two members of the board.

21-10-05. Investment director - Powers and duties.
Subject to the limitations contained in the law or the policymaking regulations or resolutions adopted by the board, the investment director may sign and execute all contracts and agreements to make purchases, sales, exchanges, investments, and reinvestments relating to the funds under the management of the board. This section is a continuing appropriation of all moneys required for the making of investments of funds under the management of the board. The investment director shall see that moneys invested are at all times handled in the best interests of the funds. Securities or investments may be sold or exchanged for other securities or investments.

The investment director shall formulate and recommend to the investment board for approval investment regulations or resolutions pertaining to the kind or nature of investments and limitations, conditions, and restrictions upon the methods, practices, or procedures for investment, reinvestment, purchase, sale, or exchange transactions that should govern the investment of funds under this chapter.

21-10-06. Funds under management of board - Accounts.
1. Subject to the provisions of section 21-10-01, the board is charged with the investment of the following funds:
   a. State bonding fund.
   b. Teachers' fund for retirement.
   c. State fire and tornado fund.
   d. Workforce safety and insurance fund.
   e. National guard tuition trust fund.
   f. Public employees retirement system.
   g. Insurance regulatory trust fund.
   h. State risk management fund.
   i. Budget stabilization fund.
   j. Health care trust fund.
   k. Cultural endowment fund.
   l. Petroleum tank release compensation fund.
   m. Legacy fund.
2. Separate accounting must be maintained for each of the funds listed in subsection 1. The moneys of the individual funds may be commingled for investment purposes when determined advantageous.
3. The state investment board may provide investment services to, and manage the money of, any agency, institution, or political subdivision of the state, subject to

agreement with the industrial commission. The scope of services to be provided by the state investment board to the agency, institution, or political subdivision must be specified in a written contract. The state investment board may charge a fee for providing investment services and any revenue collected must be deposited in the state retirement and investment fund.

21-10-06.1. Board - Investment reports.

The board shall annually prepare reports on the investment performance of each fund under its control. The reports must be uniform and must include:

1. A list of the advisory services managing investments for the board.
2. A list of investments at market value, compared to previous reporting period, of each fund managed by each advisory service.
3. Earnings, percentage earned, and change in market value of each fund's investments.
4. Comparison of the performance of each fund managed by each advisory service to other funds under the board's control and to generally accepted market indicators.

21-10-06.2. Investment costs.

The amounts necessary to pay for investment costs, such as investment counseling fees, trustee fees, custodial fees, performance measurement fees, expenses associated with money manager searches, expenses associated with onsite audits and reviews of investment managers, and asset allocation expenses, incurred by the state investment board are hereby appropriated and must be paid directly out of the funds listed in section 21-10-06 by the fund incurring the expense.

21-10-07. Legal investments.

The state investment board shall apply the prudent investor rule in investing for funds under its supervision. The "prudent investor rule" means that in making investments the fiduciaries shall exercise the judgment and care, under the circumstances then prevailing, that an institutional investor of ordinary prudence, discretion, and intelligence exercises in the management of large investments entrusted to it, not in regard to speculation but in regard to the permanent disposition of funds, considering probable safety of capital as well as probable income. The retirement funds belonging to the teachers' fund for retirement and the public employees retirement system must be invested exclusively for the benefit of their members and in accordance with the respective funds' investment goals and objectives.

21-10-08. Reserves - Percentage limitations.

In order to meet claims and liabilities, reserves must be established and maintained in each of the funds in accordance with the investment policy and asset allocation established for each fund.

21-10-09. Personal profit prohibited - Penalty.

No member, officer, agent, or employee of the state investment board may profit in any manner from transactions on behalf of the funds. Any person violating any of the provisions of this section is guilty of a class A misdemeanor.

21-10-10. State investment board fund - Cost of operation of board.

Repealed by S.L. 1989, ch. 667, § 13.

21-10-11. Legacy and budget stabilization fund advisory board.

The legacy and budget stabilization fund advisory board is created to develop recommendations for the investment of funds in the legacy fund and the budget stabilization fund to present to the state investment board. The goal of investment for the legacy fund is principal preservation while maximizing total return. The board consists of two members of the senate appointed by the senate majority leader, two members of the house of representatives appointed by the house majority leader, the director of the office of management and budget or designee, the president of the Bank of North Dakota or designee, and the tax commissioner or designee. The board shall select a chairman and must meet at the call of the chairman. The board shall report at least semiannually to the budget section. Legislative members are entitled to receive compensation and expense reimbursement as provided under section 54-03-20 and reimbursement for mileage as provided by law for state officers. The legislative council shall pay the compensation and expense reimbursement for the legislative members. The legislative council shall provide staff services to the legacy and budget stabilization fund advisory board. The staff and consultants of the state retirement and investment office shall advise the board in developing asset allocation and investment policies.

TFFR Board Responsibilities

Fay Kopp, Chief Retirement Officer

May 2013

Odd duck

- ND TFFR isn't exactly like other pension boards.
- Most of the time the Board "walks like a duck, swims like a duck, and quacks like a duck. "
- TFFR's governance structure is unique.
- Since 1989, the TFFR Board has a special relationship to the State Investment Board (SIB) through RIO.

NDRIO = TFFR + SIB

- ND Retirement and Investment Office (NDRIO) is the state agency that administers both the TFFR pension program and the SIB investment program.
- The SIB is the governing body of RIO. The TFFR Board lost its ability to hire staff in 1989 when RIO was formed. This was done in exchange for cost savings (investment and administrative); eliminate duplication of administrative functions (accounting, IT, administrative, and investments); and to expand services (benefits counseling, preretirement program, publications, etc.)
- The TFFR Board has TFFR program administrative responsibilities only, NOT RIO agency administrative responsibilities.
- The SIB has SIB program administrative responsibilities AND RIO agency administrative responsibilities.
- TFFR is BOTH an SIB investment client AND an administrative client.

RIO Created (54-52.5-01)

- *"The state retirement and investment office is created to coordinate the activities of the state investment board and teachers' fund for retirement."*

RIO Governing Authority (54-52.5-02)

- *"The SIB shall govern the state RIO. The SIB is responsible for overseeing and operating the agency and may do all things necessary to coordinate the activities of the SIB and the TFFR .*
- *The Board of trustees of the TFFR and the SIB shall maintain their legal identities and authority as otherwise provided by law."*

RIO Cost of Operation (54-52.5-03)

- *“A special fund known as the state retirement and investment fund is established for the purpose of defraying administrative expenses of the state RIO.*
- *The actual amount of administrative expenses incurred by the state RIO must be paid from the respective funds listed under section 21-10-06 and are hereby appropriated to the state RIO fund in proportion to the services rendered for each fund as estimated by the SIB.*
- *The amount necessary to pay all administrative expenses of the state RIO must be paid from the state RIO fund in accordance with the agency’s appropriation authority. Any interest income earned on the state RIO must be credited to the fund.”*

TFFR Created (15-39.1)

- State statutes outline TFFR Board composition, terms, voting, board authority, organization of board, vacancies, rulemaking power, and compensation of members.
- The TFFR Board has broad statutory authority to administer the TFFR pension program as provided for in state law.

TFFR Board composition (15-39.1-05.1)

1. *"The authority to set policy for the fund rests in a board of trustees composed as follows:*
   a. *The governor shall appoint 2 board members, who are actively employed in full time positions not classified as school administrators, from a list of 3 nominees submitted by NDEA .*
   b. *The governor shall appoint 1 board member, who is actively employed as a full-time school administrator, from a list of 3 nominees submitted by NDCEL.*
   c. *The governor shall appoint 2 board members, who are retired members of the fund, from a list of 3 nominees submitted by NDRTA.*
   d. *The state treasurer and superintendent of public instruction."*

TFFR Board authority (15-39.1-05.2)

1. *"Has the powers and privileges of a corporation, including the right to sue and be sued in its own name."*
   - In the past 30 years, TFFR has only been a party to one major lawsuit which ultimately went to the Supreme Court.
   - Other issues have been settled out of court, using the Administrative Hearings process (ALJ).

TFFR Board authority

2. *"Shall establish investment policy for the trust fund under NDCC 21-10-02.1. Investment policy must include acceptable rates of return, liquidity, and levels of risk; and long-range asset allocation targets."*

- TFFR Board determines investment guidelines. These are revisited each year as part of Chief Investment Officer's annual investment review to the TFFR Board.
- With assistance of CIO and consultants, the TFFR Board sets asset allocation policy via Asset Liability Modeling studies conducted every 5 years. Last done in 2010-11.
- SIB implements TFFR investment program utilizing asset allocation policy and investment guidelines.
- Three TFFR Board members and State Treasurer also serve on SIB.

TFFR Board authority

3. *"Shall arrange for actuarial and medical consultants. The board shall cause a qualified, competent actuary to be retained on a consulting basis."*

- TFFR Board selects consulting actuary (Segal) utilizing RFP process. Actuary provides general consulting, recommends actuarial methods and factors, conducts annual valuation, experience study (last done in 2009), and other studies as requested. Board monitors fees and work performed.
- Every 5 years, TFFR Board also selects auditing actuary via RFP process to ensure actuarial services are accurate, and to assist in monitoring consulting actuary. Last audit conducted in 2010-11 as part of transition to new actuarial consultant.
- TFFR Board utilizes services of Dr. Lunn, MedCenter One, as medical consultant. Annual fees average less than $500 per year.

TFFR Board authority

4. *"May pay benefits and consultant fees as necessary which are hereby appropriated from the fund."*

- Continuing appropriation means TFFR has blanket legislative authority to spend necessary funds for benefit payments and consulting fees.
  - Benefit payments totaled $137.7 million for FY 2012.
  - Investment expenses totaled $12.1 million.
  - Other consulting fees totaled $162,000 for FY 2012.
    - Actuary $93,800
    - Audit 39,300
    - Medical Consultant 300
    - Legal 28,600
- All payments disclosed in Comprehensive Annual Financial Report (CAFR) provided to board members and available on RIO website.
- RIO staff also reports as part of annual TFFR ends monitoring report.

TFFR Board authority

5. *“Shall submit to the legislative council’s employee benefits programs committee any necessary or desirable changes in statutes relating to the administration of the fund.”*

   - Each biennium, TFFR Board determines if legislative changes should be proposed for interim study.
   - Any proposed and approved legislation is discussed and monitored by TFFR Board through legislative updates at board meetings, legislative committee meetings, etc.

TFFR Board authority

6. *"Shall determine appropriate levels of service to be provided to members, including benefits counseling and preretirement programs."*

- Board and interest groups provide input to staff on services to be provided.
- Board monitors via personal attendance and annual reports from interest groups.
- Each year, Board receives evaluation responses and comments received directly from members and employers on outreach programs.

TFFR Board authority

7. *"Shall, through resolution, inform the state investment board, which is the administrative board of the retirement and investment office, the levels of services, goals, and objectives expected to be provided through the retirement and investment office."*
   - TFFR ends policies (which include mission, goals, services, etc) are reviewed annually by TFFR Board each July.
   - Updated TFFR ends policies are provided to SIB by inclusion in SIB Governance Manual.
   - Each year, TFFR Board completes customer satisfaction survey for SIB regarding services provided by RIO.
   - TFFR board may provide other resolutions or statements to SIB as it relates to administration of TFFR program through RIO.

Organization of TFFR Board (15-39.1-06)

1. *"The board may hold meetings as necessary for the transaction of business and a meeting may be called by the president or any two members of the board upon reasonable notice to other members of the board."*

- Regular meetings scheduled minimum 6 times per year (day preceding SIB meetings).
- Special meetings may be called from time to time as needed.
- All meetings and records open to public as prescribed by state law.

Organization of TFFR Board

2. *"The president for the ensuing year must be elected, at the first meeting following July 1 of each year."*

- TFFR Board president, and other officers elected at annual program review meeting in July.

TFFR Board Vacancies (15-39.1-07)

1. *"Vacancies which may occur among the appointed members must be filled by the governor and the appointee shall complete the term for which the original member was selected."*

- Examples: Lowell Latimer was originally appointed to complete term of Norm Stuhlmiller who passed away.
- Kim Franz was appointed to complete term of Barb Evanson who retired.
- Bob Toso was appointed to complete term of Mark Sanford who retired.

TFFR Rulemaking power (15-39.1-07)

2. *"The board may adopt such rules as may be necessary to fulfill the responsibilities of the board."*
   - Administrative rules adopted to clarify provisions in state law, outline rules and procedures to implement state law, etc.
   - Must follow procedure prescribed by Legislative Council as outlined in state law, relating to publishing notice, public hearing, comment period, TFFR Board approval.
   - Most recent rule changes adopted became effective July 1, 2012.

Compensation of TFFR members (15-39.1-08)

1. *"Members of the board, excluding ex officio members, are entitled to receive $148 as compensation per day and necessary mileage and travel expenses."*

- Pay was raised to $148 in 2011.
- Meetings less than 2 hours will receive half day of pay per board policy.
- Pay is in addition to regular salary.
- Mileage and travel expenses are according to state law.

Compensation of TFFR members

2. *“No member of the board may lose regular salary, vacation pay, vacation or any personal leave, or be denied right of attendance by the state or political subdivision while serving on official business of the fund.”*

   - Employer cannot require board member to reimburse the employer, nor reduce board member’s regular salary for compensation received from TFFR.
   - Employer must allow board member to attend board meetings, and serve on official business of TFFR.
   - Employer cannot require board member to take vacation or personal leave to attend meetings of the board.

Fiduciary Duties

Fiduciary Duties

- In general, a fiduciary is one who holds assets in trust for beneficiaries.
- TFFR board members are fiduciaries.
- TFFR Board has adopted Code of Conduct policy which outlines fiduciary responsibilities.

  See TFFR Program Policy C-3.

Fiduciary Duties

- Fiduciaries are required to discharge their duties:
  - Solely in the interest of participants and beneficiaries;
  - For the exclusive purpose of providing benefits to participants and their beneficiaries;
  - For defraying reasonable expenses of administering the system;
  - With care, skill, prudence, and diligence under circumstances then prevailing a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims; and
  - By diversifying investments of the system so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so.

What is TFFR NOT responsible for?

TFFR Board is not responsible for:

1. NDRIO general agency operations

- State Investment Board (SIB) has statutory authority to coordinate activities of SIB and TFFR and generally govern RIO.
- However, TFFR Board has statutory authority and obligation to inform the SIB, the levels of services, goals, and objectives expected to be provided through RIO.
- SIB adopted Carver policy governance model in 1995. See SIB Governance Manual for details.
- Because the TFFR Board does not have broad NDRIO agency responsibilities, the TFFR Board did not formally adopt Carver policy governance model. However, the TFFR Board follows similar governance practices where feasible. TFFR ends policies are included in SIB governance manual as the method of communicating TFFR expectations to SIB. TFFR ends policies are also included in TFFR Program manual and reviewed each year during Annual TFFR Program Review.

TFFR Board is not responsible for:

2. NDRIO agency audit
   - ND State Auditor’s Office selects external auditor to conduct NDRIO annual financial audit (currently CliftonLarsonAllen).
   - NDRIO annual audit report is presented to SIB Audit Committee. TFFR Board has at least 1 representative on Audit Committee.
   - NDRIO annual audit report is included in CAFR which is provided to each TFFR board member, and available on RIO website.
   - TFFR Board monitors NDRIO financial audit and TFFR program audits through annual monitoring reports from RIO audit and fiscal/accounting staff.

TFFR Board is not responsible for:

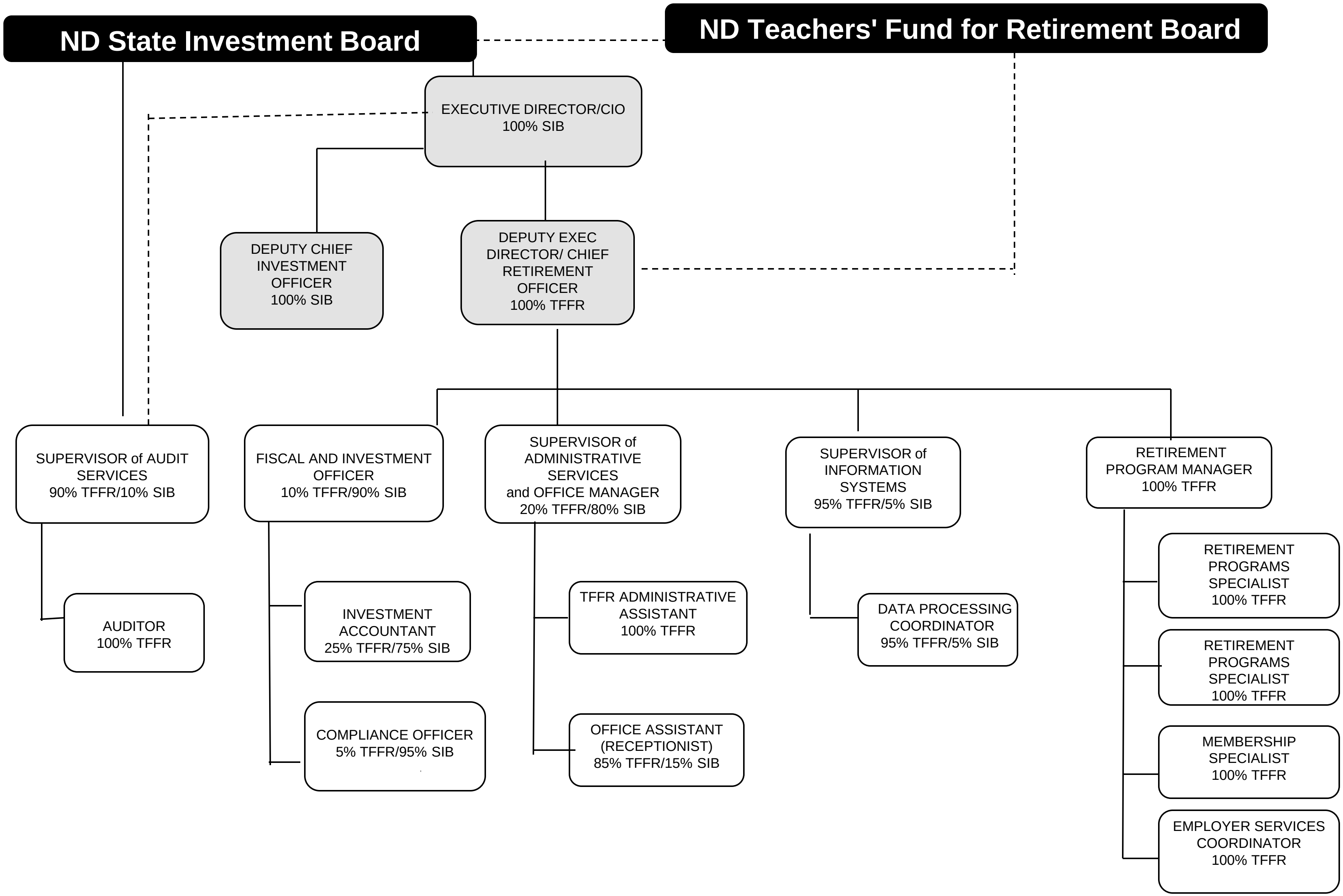
3. ND RIO agency budget
   - Budget developed by NDRIO staff (Supervisor of Fiscal Management) under direction of Executive Director/Chief Investment Officer and Deputy Executive Director/Chief Retirement Officer to ensure sufficient budget resources are available for both programs.
   - Budget is divided between two programs:

     TFFR retirement program and SIB investment program.
   - Executive Director approves NDRIO budget to be submitted to Legislature, per SIB governance policy.
   - Legislature approves budget.
   - TFFR Board monitors NDRIO budget through annual budget monitoring reports from NDRIO fiscal staff.

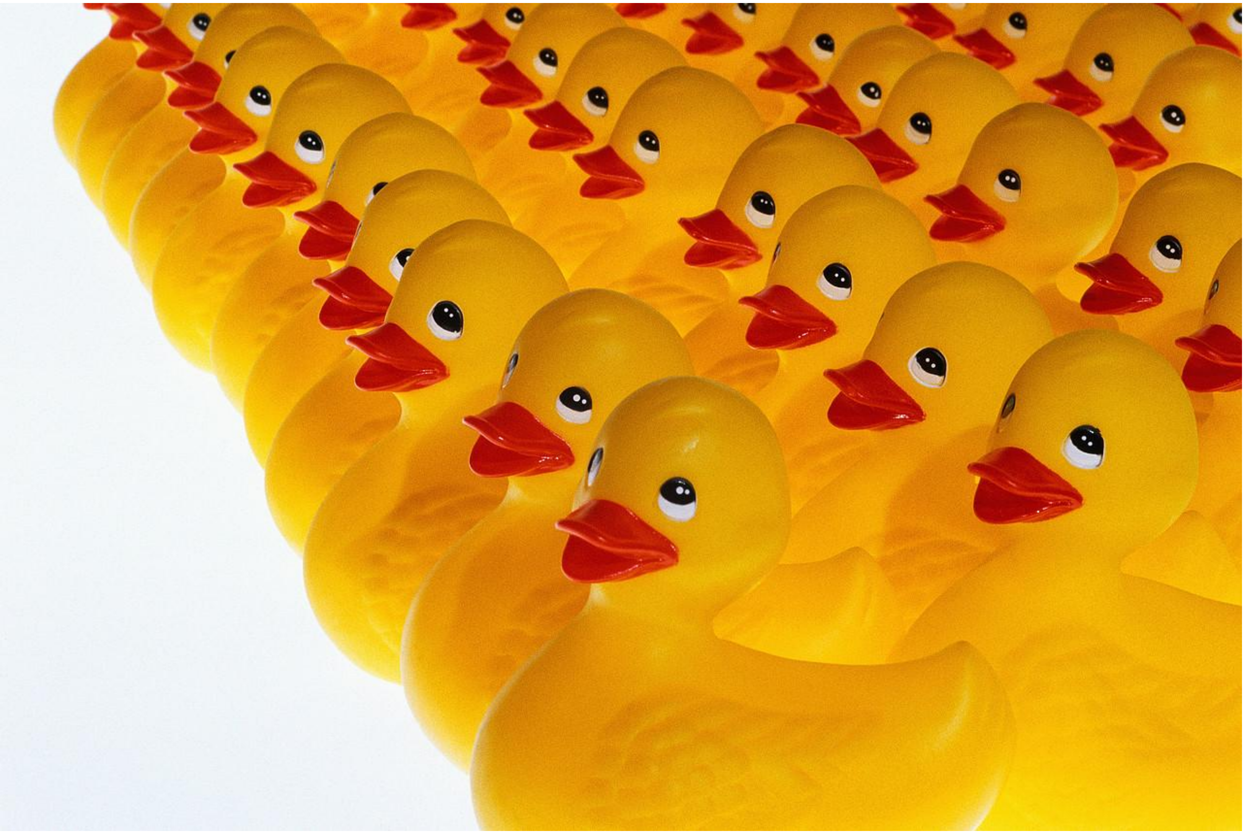
TFFR Board is not responsible for:

4. ND RIO agency staff
   - Per SIB governance model, SIB is responsible for hiring, annual evaluation, and setting pay for Executive Director/ Chief Investment Officer who serves at pleasure of SIB.
   - Executive Director/CIO is responsible for the hiring, annual evaluation, and setting pay for Deputy Executive Director/Chief Retirement Officer. Input may be solicited from TFFR Board, member and employer interest groups, etc. at the discretion of the Executive Director.
   - Executive Director/CIO is responsible for the hiring, termination, and annual evaluation of all other NDRIO staff. This is done in conjunction with, or based on recommendations from, the Dep. Exec Director/Chief Retirement Officer for TFFR related staff. Pay for classified employees is set per state personnel guidelines.

ND Retirement and Investment Office (RIO)
Agency Organizational Chart (January 2012)



Keeping Our Ducks in a Row



MEMORANDUM

TO: **TFFR Board**

FROM: **Fay Kopp**

DATE: **May 9, 2013**

SUBJ: **Deputy Executive Director/Chief Retirement Officer position**

Enclosed are copies of TFFR by-laws which provide a general outline of the Deputy Executive Director/Chief Retirement Officer responsibilities and duties. These by-laws are included in the TFFR program manual which is reviewed by the TFFR Board each July during the Annual TFFR Program Review.

At the March meeting, the Board asked staff to present options relating to how the Board could provide input to the Executive Director/Chief Investment Officer on performance evaluations and employment decisions affecting the Deputy Executive Director/Chief Retirement Officer position.

Jan and I have reviewed this issue and will present some options for consideration. While changes to TFFR and/or SIB policies may be suggested, no changes to state statutes or RIO's organizational structure would be required.

Enclosures

D. By-Laws

Page

TFFR Board Adopted: May 25, 1995.
Amended: August 21, 1997; November 18, 1999; September 20, 2007; September 25, 2008; September 23, 2010; September 22, 2011.

Chapter 3 – Officers and Duties (continued)

Section 3-5. **Deputy Executive Director – Retirement Officer.** The Deputy Executive Director/Retirement Officer will be hired by the Executive Director, serve in an unclassified position at the Executive Director's pleasure, and will be paid such salary as the Executive Director determines.

3-5-1. The Deputy Executive Director/Retirement Officer assists the Executive Director in planning, supervising, and directing overall RIO programs in accordance with the SIB governance policies and state laws and rules and represents the Executive Director in his/her absence.

3-5-2. The Deputy Executive Director/Retirement Officer administers the retirement program in accordance with governing statutes and board policies established by the TFFR board and performs related work as assigned by that board.

3-5-3. The Deputy Executive Director/Retirement Officer develops annual and long-range plans for the board. He/she interprets state and federal law, which governs the retirement program and develops administrative rules, policies, and procedures necessary to administer the program.

3-5-4. The Deputy Executive Director/Retirement Officer represents the TFFR board on retirement program issues.

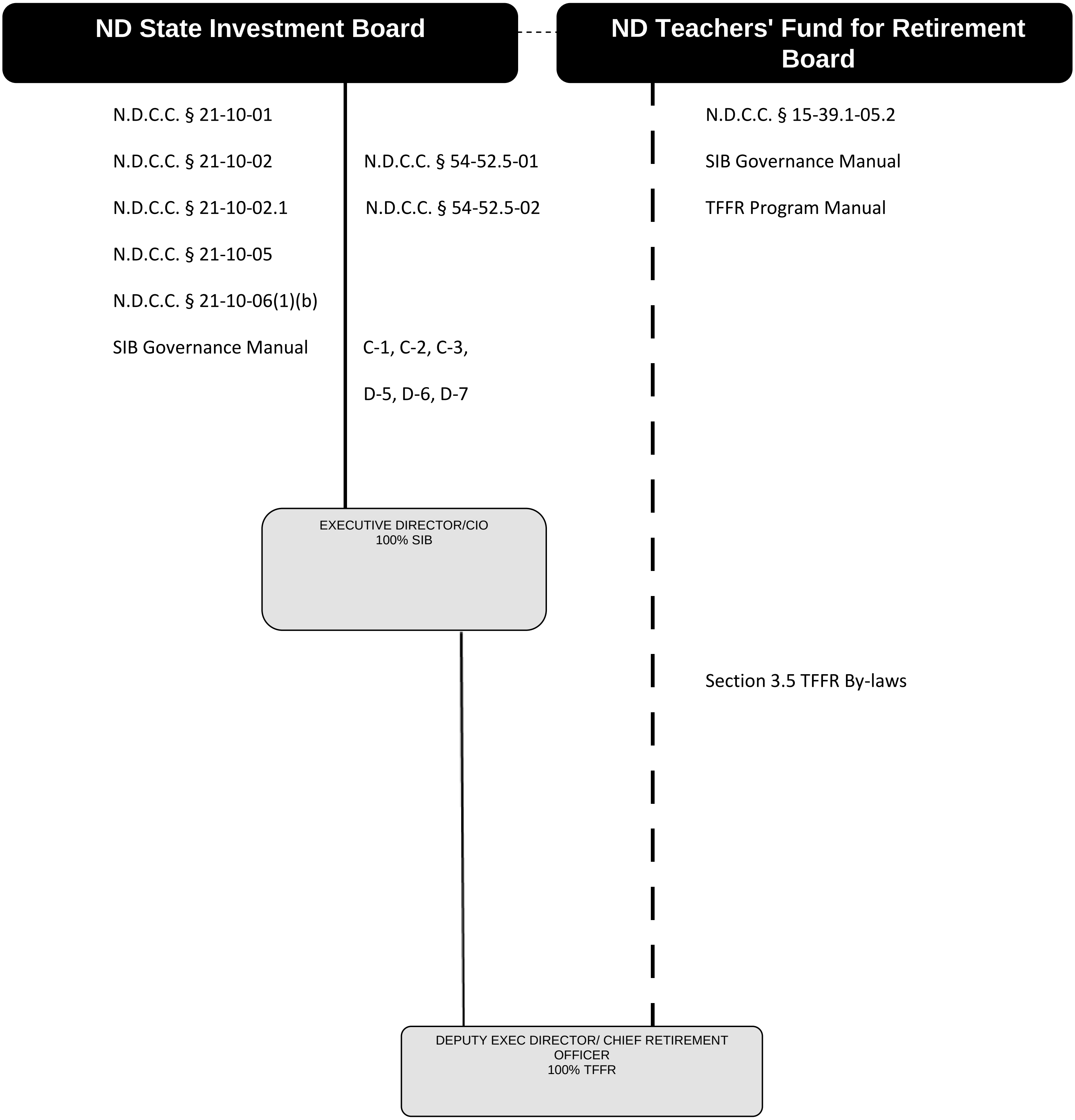
3-5-5. The Deputy Executive Director/Retirement Officer works as a team with the TFFR board, interest groups, legislative committees, actuarial consultants, legal counsel, and others to administer the retirement program.

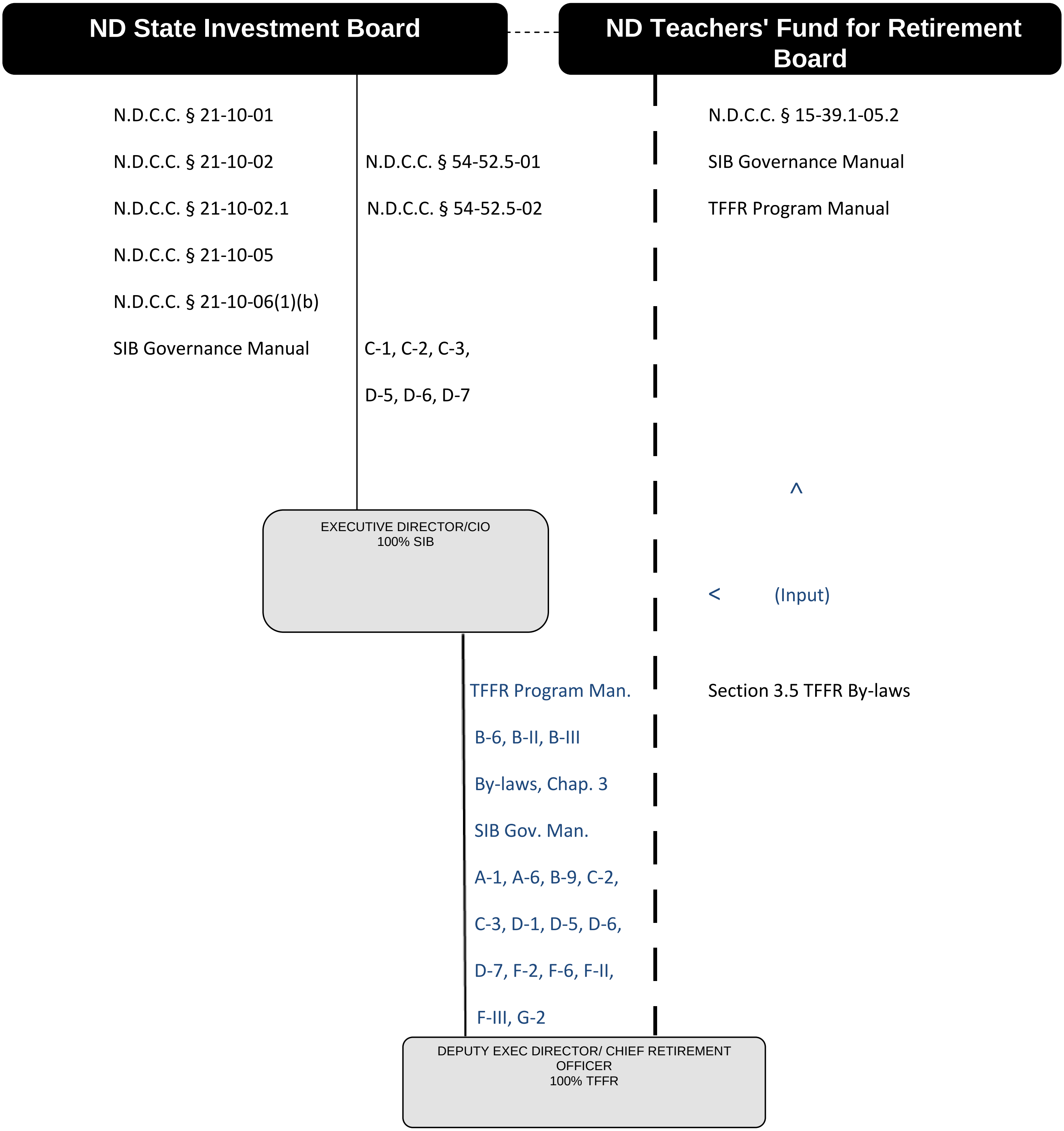
3-5-6. The Deputy Executive Director/Retirement Officer will assist in the formulation of RIO's budget, including staffing needs, program costs, operating costs, and information technology requirements to assure that retirement program obligations are met.

3-5-7. The Deputy Executive Director/Retirement Officer is the custodian of the books, records, and files of TFFR. He/She will attend all meetings of the TFFR board, is responsible for board meeting minutes, required notices, procedures of the board, and applicable rules and regulations of the fund.

3-5-8. The Deputy Executive Director - Retirement Officer will keep a correct roster of the membership of the fund, the salaries paid to each member for service as a teacher, when and what teachers are dropped or withdrawn from the fund, and records of all pensions paid.

3-5-9. The Deputy Executive Director - Retirement Officer will process all applications for claims for payment as allowed under state laws in a timely manner.


ND State Investment Board
ND Teachers' Fund for Retirement Board
N.D.C.C. § 21-10-01
N.D.C.C. § 21-10-02
N.D.C.C. § 21-10-02.1
N.D.C.C. § 21-10-05
N.D.C.C. § 21-10-06(1)(b)
SIB Governance Manual
N.D.C.C. § 54-52.5-01
N.D.C.C. § 54-52.5-02
C-1, C-2, C-3,
D-5, D-6, D-7
N.D.C.C. § 15-39.1-05.2
SIB Governance Manual
TFFR Program Manual
EXECUTIVE DIRECTOR/CIO
100% SIB
Section 3.5 TFFR By-laws
DEPUTY EXEC DIRECTOR/ CHIEF RETIREMENT OFFICER
100% TFFR


ND State Investment Board
ND Teachers' Fund for Retirement Board
N.D.C.C. § 21-10-01
N.D.C.C. § 21-10-02
N.D.C.C. § 21-10-02.1
N.D.C.C. § 21-10-05
N.D.C.C. § 21-10-06(1)(b)
SIB Governance Manual
N.D.C.C. § 54-52.5-01
N.D.C.C. § 54-52.5-02
C-1, C-2, C-3,
D-5, D-6, D-7
N.D.C.C. § 15-39.1-05.2
SIB Governance Manual
TFFR Program Manual
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EXECUTIVE DIRECTOR/CIO
100% SIB
TFFR Program Man.
B-6, B-II, B-III
By-laws, Chap. 3
SIB Gov. Man.
A-1, A-6, B-9, C-2,
C-3, D-1, D-5, D-6,
D-7, F-2, F-6, F-II,
F-III, G-2
Section 3.5 TFFR By-laws
DEPUTY EXEC DIRECTOR/ CHIEF RETIREMENT OFFICER
100% TFFR

SAMPLE

Recommendations for SIB Governance
Policy changes

POLICY TYPE: EXECUTIVE LIMITATIONS

POLICY TITLE: *COMMUNICATION AND COUNSEL TO THE BOARD*

With respect to providing information and counsel to the board, the executive director may not permit the board to be uninformed.

Accordingly, the executive director may not:

1. Neglect to submit monitoring data required by the board (see policy on Monitoring Executive Performance) in a timely, accurate, and understandable fashion, directly addressing provisions of the board policies being monitored.

2. Let the board be unaware of relevant trends, anticipated adverse media coverage, material external and internal changes, and particularly changes in the assumptions upon which any board policy has previously been established.

3. Fail to advise the board if, in the executive director's opinion, the board is not in compliance with its own policies on *Governance Process* and *Board-Staff Relationship*, particularly in the case of board behavior which is detrimental to the work relationship between the board and the executive director.

4. Fail to marshal for the board as many staff and external points of view, issues, and options as needed for fully informed board choices.

5. Present information in unnecessarily complex or lengthy form.

6. Fail to provide a mechanism for official board, officer, or committee communications.

7. Fail to deal with the board as a whole except when (a) fulfilling individual requests for information or (b) responding to officers or committees duly charged by the board.

8. Fail to report in a timely manner an actual or anticipated noncompliance with any policy of the board, particularly *Ends* and *Executive Limitations*.

9. Fail to inform the SIB and TFFR boards in a timely manner of any intention to hire or dismiss the Deputy Executive Director/ Chief Retirement Officer.

10. Fail to keep the board informed concerning the delegation of fiduciary authority to any staff member. Every person to whom such fiduciary responsibility is delegated is ultimately accountable to the board as to the exercise and execution of the delegated authority.

Comment [WU1]: Supported by SIB Governance Manual A-1 (5) & (8), C-2,C-3,D-1,D-5,D-6,D-7,F-2,F-6, F-II, F-III, G-2 (Chapt. 2 by-laws); and TFFR Program Manual B-6, B-II, B-III and Chapt. 3 by-laws.

Policy Implemented: June 23, 1995; November 19, 1999.

POLICY TYPE: BOARD-STAFF RELATIONSHIP

POLICY TITLE: *DELEGATION TO THE EXECUTIVE DIRECTOR*

All board authority delegated to staff is delegated through the executive director.

1. The board authority will direct the executive director to achieve specified results, for specified recipients, at a specified cost through the establishment of *Ends* policies. The board will limit the latitude the Executive Director may exercise in practices, methods, conduct, and other "means" to the *Ends* through establishment of *Executive Limitations* policies.

2. The Executive Director must use reasonable judgment in the implementation or administration of the board's *Ends* and *Executive Limitations* policies; the executive director is authorized to establish practices, and develop activities.

3. The board may change its *Ends* and *Executive Limitations* policies. By so doing, the board changes the latitude of choice given to the Executive Director. If any particular delegation is in place, the board and its members will respect and support the Executive Director's choices, provided that the Executive Director's choice is consistent with the board's fiduciary responsibility.

4. Only decisions of the board acting as the body are binding upon the Executive Director.
    a. Decisions or instructions of individual board members, officers, or committees are not binding on the Executive Director except in rare instances when the board has specifically authorized such exercise of authority.
    b. In the case of board members or committees requesting information, other than a public record, or assistance without board authorization, the Executive Director may refuse such requests that require a material amount of staff time or funds or is disruptive.

5. The Executive Director will be responsible for the hiring, termination, and annual evaluation of all employees of the Retirement and Investment Office. With regards to the Deputy Executive Director/ Chief Retirement Officer, the Executive Director shall solicit input from the TFFR Board prior to the hiring, termination, and the annual evaluation of that position.

Policy Implemented: June 23, 1995.
Amended: November 22, 1996; November 19, 1999.

Comment [WU2]: Supported by SIB Governance Manual B-9(4),C-3, D-1, D-5, D-6, D-7, F-2, F-6, F-II, F-III, G-2 (Chapt. 2 by-laws); and TFFR Program Manual B-6, B-II, B-III, Chapt. 3 by-laws.

Exhibit B-II

Teachers' Fund for Retirement Responsibilities

1. Establish policies for the administration of the TFFR programs.

2. Submit legislation, monitor the statutory responsibilities of the TFFR programs as outlined in the NDCC, and promulgate Administrative Rules.

3. Establish and monitor actuarial assumptions used to value the retirement plan and to conduct periodic valuations.

4. Establish and monitor retirement benefit and service program goals.

5. Establish and monitor policy for investment goals, objectives, and asset allocation for the fund.

6. Communicate and monitor program and personnel expectations with the SIB.

Comment [WU1]: Supported by TFFR Program Manual B-6, B-III, and Chapt. 3 by-laws; NDCC 15-39.1-05.2; and SIB Governance Manual B-9(4), C-3, D-1, D-5, D-6, D-7, F-2, F-6, F-II, F-III, G-2 (Chapt. 2 by-laws).

TFFR Board Adopted: May 25, 1995.

Chapter 3 – Officers and Duties

Section 3.1. The officers of the board will be the President, Vice President, Executive Director, and Deputy Executive Director/Retirement Officer. The President and Vice President will be elected by the board immediately following July 1 of each year and will hold office for one year or until their successors are elected and qualified. A vacancy occurring with the President or Vice President will be filled by the board at the first meeting of the board following the vacancy. The Executive Director and Deputy Executive Director/Retirement Officer will not be voting members of the board.

Section 3-2. **President.** The President will preside at all meetings of the board. The President will be an ex officio member of all board committees created from time to time. The President will approve the board meeting agenda, and with the Deputy Executive Director/Retirement Officer and Executive Director execute all instruments required to be executed on behalf of the fund, and will perform such other duties as may be imposed by the board.

Section 3-3. **Vice President.** The Vice President will perform the duties of the President in his/her absence.

Section 3-4. **Executive Director.** The Executive Director will be hired by the SIB, serve in an unclassified position at that board's pleasure, and will be paid such salary as the SIB determines.

3-4-1. The Executive Director oversees planning, supervising, and directing overall RIO programs in accordance with the SIB governance policies and state laws and rules.

3-4-2. The Executive Director administers the investment program of RIO and performs related work as assigned by the SIB.

3-4-3. The Executive Director directs the preparation and execution of the RIO budget and legislative agenda and evaluates and monitors financial and operational programs.

3-4-4. The Executive Director represents RIO, promotes RIO programs, and has the authority and responsibility to carry out the day-to-day administrative duties for RIO.

3-4-5. The Executive Director attends all meetings of the SIB and TFFR Board.

3-4-6. The Executive Director hires the Deputy Executive Director/ Retirement Officer and other staff as necessary to carry out the responsibilities of RIO.

~~3-4-6.~~3-4-7. The Executive Director shall solicit input from the TFFR Board prior to hiring, termination, or the annual evaluation of the Deputy Executive Director/ Chief Retirement Officer.

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Comment [WU2]: Supported by TFFR Program Manual B-6, B-II, B-III, Chapt. 3 by-laws; NDCC 15-39.1-05.2; and SIB Governance Manual B-9(4), C-3, D-1, D-5, D-6, D-7, F-2, F-6, F-II, F-III, G-2 (Chapt. 2 by-laws).

TFFR OPTIONS RE: METHODS OF COMMUNICATION TO SIB

1. BY RESOLUTION:

N.D.C.C. § 15-39.1-05.2

The board:

7. Shall, through resolution, inform the state investment board, which is the administrative board of the retirement and investment office, the levels of services, goals, and objectives expected to be provided through the retirement and investment office.

2. BY FORMAL REQUEST:

Updates to TFFR Program Manual and/or SIB Governance Manual

3. BY INFORMAL REQUEST:

Rely on existing provisions of TFFR Program Manual and SIB Governance Manual.

4. NO ACTION:

Determine that current level of communication is sufficient to meet statutory obligations and fiduciary responsibilities.

SAMPLE

MEMORANDUM

TO: TEACHERS' FUND FOR RETIREMENT BOARD

FROM: SCOTT ENGMANN (1997, 98 and 99)
STEVE COCHRANE (2000, 01 and 02)

DATE: MAY ____________

RE: ANNUAL JOB PERFORMANCE REVIEW OF FAY KOPP

It is once again time to complete an annual job performance review of Fay. I need your assistance in order to give Fay a complete job performance evaluation. If each of you would answer the following questions, I will be able to give her a composite of your responses showing her how her performance as Retirement Officer is viewed.

PLEASE COMPLETE AND RETURN TO ME BY JUNE __________. THANKS.

1. How do you rate communication between Fay and the Board?

____Excellent (3) ____Good (2) ____Adequate (1) ____Below Expectation (0)

Comment:

2. How do you rate the written materials Fay prepares for board meetings?

____Well Written (2) ____Adequate (1) ____Poor (0)

Comment:

3. How do you rate Fay's knowledge of our retirement plan and the public pension field?

____Excellent (3) ____Good (2) ____Adequate (1) ____Below Expectation (0)

Comment:

4. How do you rate your confidence in the recommendations Fay gives to the Board for our retirement program?

_____Very Confident (2) _____Confident (1) _____Not Confident (0)

Comment:

5. How do you rate Fay's overall job performance?

_____ Above Expectations (2) _____Meets Expectations (1) _____Below Expectation (0)

Comment:

6. What other job performance issues would you like to comment on?

MEMORANDUM

TO: **TFFR Board**

FROM: **Fay Kopp**

DATE: **May 9, 2013**

SUBJ: **Board Resolutions**

As you know, Bob Toso plans to retire as Superintendent of Jamestown Public Schools effective June 30, 2013. Bob served on the TFFR Board for 6 years. Due to his retirement, he will no longer be eligible to represent active school administrators on the Board.

Additionally, Lowell Latimer's term on the TFFR Board ends June 30, 2013, and he does not plan to seek re-appointment. Therefore, there will also be a retired member vacancy on the Board. Lowell served on the Board for 9 years.

I have drafted the enclosed resolutions for the TFFR Board's consideration in recognition of Bob and Lowell's distinguished service on the TFFR Board.

The Governor's office has been informed of these upcoming vacancies, and NDCEL and NDRTA have been notified to submit names to the Governor's office for consideration. To date, I have not heard of any new appointments.

Since the May meeting will be Bob and Lowell's last TFFR Board meeting, we will host a Retirement Coffee Party in their honor during the meeting break.

Enclosures

ND TFFR Board Resolution
in Appreciation of
Lowell F. Latimer

WHEREAS, Dr. Lowell Latimer served as trustee and vice president of the ND Teachers' Fund for Retirement Board representing retired members with distinction for 9 years, from 2004 to 2013; and

WHEREAS, Dr. Latimer has honorably served the education community in a career spanning more than four decades having worked as a teacher, principal, and administrator in Minot and Minot area schools until his retirement in 1993, and as director of the Minot Public School Foundation since his retirement; and

WHEREAS, Dr. Latimer has been actively involved in numerous professional, civic, community, church, and state activities and associations; and

WHEREAS, Dr. Latimer has been a passionate defender of defined benefit plans and their ability to provide retirement security, and has been dedicated to protecting the interests of the pension system and its active and retired members; and

WHEREAS, Dr. Latimer has provided thoughtful guidance and leadership on pension issues, supported efforts to strengthen TFFR's funding structure and safeguard the financial integrity of the fund, and was fully dedicated to the mission of the Fund; and

WHEREAS, Dr. Latimer has distinguished himself as a knowledgeable and experienced trustee whose commitment to integrity and excellence have earned him the respect of those who have worked with him; now therefore, be it

RESOLVED, that the TFFR Board express its heartfelt thanks to Dr. Latimer for his energetic and compassionate service to the Board, and for his legacy of trust, respect, and caring for others; and be it further

RESOLVED, that the Board wishes Dr. Latimer, and his wife, Ann, good health and happiness in their retirement; and be it further

RESOLVED, that a copy of this Resolution be presented to Dr. Latimer, printed in the official TFFR Board minutes, and submitted to the National Council on Teacher Retirement, on behalf of the many lives he has so positively touched.

DATED this 16th day of May, 2013

Mike Gessner, President	Robert Toso, Trustee
Kim Franz, Trustee	Clarence Corneil, Trustee
Kelly Schmidt, State Treasurer	Kirsten Baesler, State Superintendent

ND TFFR Board Resolution
in Appreciation of
Robert B. Toso

WHEREAS, Mr. Robert (Bob) Toso served as trustee of the ND Teachers' Fund for Retirement Board representing school administrators with honor for 6 years, from 2007 until his retirement in 2013; and

WHEREAS, Mr. Toso also honorably served as trustee of the ND State Investment Board representing TFFR members during his tenure; and

WHEREAS, Mr. Toso dedicated his professional career to the ND education community for 37 years as teacher, coach, principal, assistant superintendent, and superintendent in the school districts of Pingree, Rolette, Glenburn, New Rockford, Valley City, and Jamestown; and

WHEREAS, Mr. Toso has been actively involved in many professional, civic, community, church, and state activities and associations; and

WHEREAS, Mr. Toso has been a zealous defender of pension security for ND educators and has earned a reputation as a strong advocate for defined benefit plans, cost efficient pension administration, and high-quality customer service; and

WHEREAS, Mr. Toso provided steadfast leadership on pension issues, and supported efforts to strengthen TFFR's funding structure, prudently invest trust fund assets, and safeguard the financial integrity of the fund; and

WHEREAS, Mr. Toso has distinguished himself as an outstanding trustee whose invaluable knowledge, experience, integrity, and compassion has served trust fund members with respect; now therefore, be it

RESOLVED, that the TFFR Board express its sincere appreciation to Mr. Toso for his dedicated service to the Board, and for his positive leadership and unwavering support of educators, students, and citizens of North Dakota; and be it further

RESOLVED, that the Board extends its best wishes to Mr. Toso, and his wife, Alaine, for a long and happy retirement; and be it further

RESOLVED, that a copy of this Resolution be presented to Mr. Toso, printed in the official TFFR Board minutes, and submitted to the National Council on Teacher Retirement, on behalf of the many lives he has so positively touched.

DATED this 16th day of May, 2013

Mike Gessner, President	Lowell Latimer, Vice President
Kim Franz, Trustee	Clarence Corneil, Trustee
Kelly Schmidt, State Treasurer	Kirsten Baesler, State Superintendent

MEMORANDUM

TO: **TFFR Board**

FROM: **Gary Vetter**

DATE: **May 16, 2013**

SUBJ: **Annual Technology Report**

1. 2011 legislative changes:

   For the past two years, the main IT priority has been coordinating the development, testing, and implementation of CPAS pension software modifications required for 2011 legislative changes (7-2012 and 7-2014 contribution increases and 7-2013 benefit changes). As of this date, programming changes are complete or near completion. System modifications are scheduled to go into production this summer. Thanks to Shelly Schumacher (Retirement Program Manager) and Rich Nagel (IT Coordinator) on this important project.

2. Member Web Services

   Due to budget constraints and the programming and testing effort required for 2011 legislative changes, the Member Web Services project was put on hold. We expect to resume programming later this year, after completion of 2011 legislative implementation (above) and fiscal year end tasks.

3. Employer Web Services

   Of 220 active employers, 140 (64%) are reporting via Employer Web Services. All of the 10 largest schools are reporting via web. Of the 80 employers not reporting via internet, 32 had fewer than 10 members. Of 10,894 members reported, 9,671 (89%) are reported via Employer Web Services.

   Last year, 55% of active employers and 84% of members were reported via the web. Thanks again to Tami Volkert (Employer Services Coordinator) and Rich Nagel (IT Coordinator) for encouraging employers to switch to electronic reporting.

4. Agency desktop computers

   There is no change from last year's report. RIO staff will receive Windows 8 (64-bit) computers in accordance with our 4-year replacement cycle in 2015.

5. Agency portable computers

   According to our 3-year portable computer replacement schedule, they will be replaced late in 2014. We will revisit the rationale for the shorter replacement cycle; if the end-users are satisfied with performance, and the computers do not show excessive wear and tear, we would consider using them an additional year. Based on our experience with the current laptops, we expect this may be possible.

6. Disaster Recovery

   Leslie Moszer, Compliance Officer, has kept RIO's disaster recovery plan updated. Rich has contributed documentation updates. We will retest when we have our next personnel change (probably new CEO).

7. Records retention and purging

   We ran scripts to delete data from the CPAS database in accordance with our records retention schedule (compiled by Bonnie Heit).

8. System security

   NDRIO security policy is set in compliance with guidelines established by the state information technology department (ITD). The laptop computers used by the retirement program specialists are now using a hard drive encryption system managed by ITD.

Status of other IT updates:

1. CPAS Oracle database management system upgraded to version 11g. Our database is now at the latest level supported by ITD.
2. IBM WebSphere upgraded to version 8. Our online services can take advantage of the most recent internet application server technology.
3. We are in the process of converting our computer management system to Microsoft System Center Configuration Manager (SCCM). When this is complete, our IT division will be able to provision and configure our electronic devices from a central console.
4. Network configuration for Tamale Research Management System (RMS) is complete. NDSIB staff members will use Tamale to automatically centralize and categorize content from email, research notes, and other sources, and present the content in a format for decision making.

Future IT directions:

1. Replace current workgroup laser printer.
2. Wireless access point in RIO office.
3. Investigate possibilities for utilization of state network infrastructure (e.g. webinars).
4. Evaluate current web site for redesign and usability on tablets and smartphones.
5. Electronic documents for board members.

ND TEACHERS FUND FOR RETIREMENT
INVESTMENT PERFORMANCE REPORT AS OF MARCH 31, 2013

	March-13							December-12					September-12					Current Fiscal YTD		Prior FY12		3 Years Ended 6/30/2012		5 Years Ended 6/30/2012
		Allocation		Quarter		Month			Allocation		Quarter			Allocation		Quarter								
	Market Value	Actual	Policy	Gross (8)	Net	Gross (8)	Net	Market Value	Actual	Policy	Gross (8)	Net	Market Value	Actual	Policy	Gross (8)	Net	Gross (7)	Net	Gross (7)	Net	Gross	Net	Net
TOTAL FUND	1,793,999,762	100.0%	100.0%	4.69%	4.61%	1.73%	1.70%	1,721,114,269	100.0%	100.0%	2.89%	2.80%	1,683,110,433	100.0%	100.0%	4.53%	4.44%	12.59%	12.31%	-0.62%	-0.97%	12.29%	11.88%	-1.23%
POLICY TARGET BENCHMARK				4.77%	4.77%	1.53%	1.53%				2.16%	2.16%				4.37%	4.37%	11.72%	11.72%	-0.82%	-0.82%	11.17%	11.17%	1.19%
ATTRIBUTION ANALYSIS																								
Asset Allocation				0.02%	0.02%	0.02%	0.02%				-0.01%	-0.01%				0.01%	0.01%	0.03%	0.03%	0.27%	0.27%			
Manager Selection				-0.11%	-0.19%	0.18%	0.16%				0.73%	0.64%				0.14%	0.06%	0.84%	0.56%	-0.07%	-0.43%			
TOTAL RELATIVE RETURN				-0.09%	-0.17%	0.20%	0.18%				0.72%	0.64%				0.16%	0.07%	0.87%	0.59%	0.20%	-0.16%			
GLOBAL EQUITIES	1,054,873,096	58.8%	57.0%	7.53%	7.44%	2.59%	2.56%	991,157,414	57.6%	57.0%	2.80%	2.71%	975,918,182	58.0%	57.0%	5.81%	5.72%	16.96%	16.66%					
Benchmark				7.40%	7.40%	2.27%	2.27%				2.68%	2.68%				6.01%	6.01%	16.91%	16.91%					
Epoch (1)	86,292,910	4.8%	4.5%	7.88%	7.63%	2.98%	2.96%	78,948,234	4.6%	4.5%	2.68%	2.43%	77,035,363	4.6%	4.5%	4.91%	4.66%	16.21%	15.38%	-1.33%	-2.28%	11.26%	10.15%	0.02%
Calamos	24,489,756	1.4%	1.5%	4.03%	3.84%	1.45%	1.44%	23,228,979	1.3%	1.5%	0.10%	-0.08%	23,245,618	1.4%	1.5%	6.14%	5.95%	10.54%	9.94%	N/A	N/A	N/A	N/A	N/A
LSV	180,419,640	10.1%	10.0%															N/A	N/A					
Total Global Equities	291,202,306	16.2%	16.0%	6.89%	6.75%	2.62%	2.60%	102,177,213	5.9%	6.0%	2.08%	1.85%	100,280,981	6.0%	6.0%	5.19%	4.96%	14.78%	14.11%					
MSCI World (2)				7.73%	7.73%	2.34%	2.34%				2.49%	2.49%				6.71%	6.71%	17.82%	17.82%					
Domestic - broad	410,969,343	22.9%	21.5%	11.89%	11.80%	4.41%	4.39%	472,195,950	27.4%	27.4%	0.82%	0.73%	472,834,867	28.1%	27.4%	6.22%	6.13%	19.83%	19.53%					
Benchmark				11.29%	11.29%	4.03%	4.03%				0.51%	0.51%				6.08%	6.08%	18.66%	18.66%					
Large Cap Domestic																								
LA Capital	118,343,647	6.6%	5.0%	10.79%	10.73%	4.56%	4.55%	106,051,999	6.2%	6.7%	-1.61%	-1.66%	109,445,344	6.5%	6.7%	5.74%	5.69%	15.26%	15.08%	6.79%	6.56%	17.64%	17.43%	2.00%
Russell 1000 Growth				9.54%	9.54%	3.75%	3.75%				-1.32%	-1.32%				6.11%	6.11%	14.70%	14.70%	5.76%	5.76%	17.50%	17.50%	2.87%
LSV	-	0.0%	0.0%	N/A	N/A	N/A	N/A	112,056,980	6.5%	6.7%	3.35%	3.27%	108,316,199	6.4%	6.7%	7.51%	7.43%	N/A	N/A	-1.21%	-1.51%	15.39%	15.02%	-3.25%
Russell 1000 Value				12.31%	12.31%	3.96%	3.96%				1.52%	1.52%				6.50%	6.50%	21.43%	21.43%	3.00%	3.00%	15.80%	15.80%	-2.19%
LA Capital	80,822,648	4.5%	2.9%	11.14%	11.08%	4.30%	4.28%	72,184,062	4.2%	3.8%	-0.40%	-0.45%	73,757,095	4.4%	3.8%	5.41%	5.36%	16.68%	16.51%	6.37%	6.15%	17.26%	16.97%	0.99%
Russell 1000				10.96%	10.96%	3.86%	3.86%				0.12%	0.12%				6.31%	6.31%	18.11%	18.11%	4.37%	4.37%	16.64%	16.64%	0.39%
Northern Trust	40,701,173	2.3%	2.3%	12.23%	12.12%	4.41%	4.38%	36,010,671	2.1%	2.1%	-0.81%	-0.91%	36,231,281	2.2%	2.2%	7.05%	6.95%	19.17%	18.83%	6.46%	6.05%	16.89%	16.74%	0.00%
Prudential	-	0.0%	0.0%	N/A	N/A	N/A	N/A	-	0.0%	0.0%	N/A	N/A	163,192	0.0%	0.0%	0.00%	-0.04%	N/A	N/A	6.42%	6.25%	30.88%	30.72%	N/A
Clifton	73,641,970	4.1%	6.5%	10.60%	10.54%	3.77%	3.74%	36,013,077	2.1%	1.9%	-0.27%	-0.33%	36,576,554	2.2%	1.9%	6.56%	6.49%	17.55%	17.32%	6.57%	6.30%	N/A	N/A	N/A
S&P 500				10.61%	10.61%	3.75%	3.75%				-0.38%	-0.38%				6.35%	6.35%	17.19%	17.19%	5.45%	5.45%	16.40%	16.40%	0.22%
Total Large Cap Domestic	313,509,439	17.5%	16.6%	11.58%	11.51%	4.23%	4.21%	362,316,788	21.1%	21.2%	0.34%	0.27%	364,489,664	21.7%	21.2%	6.40%	6.33%	19.12%	18.90%	3.68%	3.35%	17.27%	16.86%	-4.31%
Russell 1000 (2)				10.96%	10.96%	3.86%	3.86%				0.12%	0.12%				6.31%	6.31%	18.11%	18.11%	5.34%	5.34%	16.36%	16.36%	0.20%
Small Cap Domestic																								
SEI	218,010	0.0%	0.0%	-2.69%	-2.69%	-4.89%	-4.89%	354,211	0.0%	0.0%	371.62%	371.62%	75,044	0.0%	0.0%	-0.49%	-0.49%	356.68%	356.68%	-27.98%	-27.98%	-3.92%	-4.12%	-17.53%
Callan	50,034,403	2.8%	2.4%	13.34%	13.13%	5.11%	5.04%	54,860,069	3.2%	3.1%	2.17%	1.97%	53,743,850	3.2%	3.1%	5.14%	4.94%	21.76%	21.05%	-3.11%	-3.87%	19.05%	18.33%	0.63%
Clifton	47,207,491	2.6%	2.4%	12.42%	12.31%	4.54%	4.50%	54,664,882	3.2%	3.1%	2.15%	2.05%	54,526,309	3.2%	3.1%	6.12%	6.01%	21.88%	21.49%	-0.63%	-1.05%	N/A	N/A	N/A
Total Small Cap Domestic	97,459,904	5.4%	4.8%	12.88%	12.71%	4.83%	4.78%	109,879,162	6.4%	6.2%	2.42%	2.27%	108,345,204	6.4%	6.2%	5.63%	5.47%	22.12%	21.57%	0.23%	-0.37%	23.45%	22.72%	-0.06%
Russell 2000				12.39%	12.39%	4.62%	4.62%				1.85%	1.85%				5.25%	5.25%	20.49%	20.49%	-2.08%	-2.08%	17.80%	17.80%	0.54%
International - broad	257,881,616	14.4%	14.5%	4.08%	3.94%	0.70%	0.66%	317,695,185	18.5%	18.6%	6.67%	6.53%	299,730,142	17.8%	18.6%	7.22%	7.07%	19.04%	18.55%					
Benchmark				3.83%	3.83%	0.34%	0.34%				6.39%	6.39%				7.09%	7.09%	18.29%	18.29%					
Developed International																								
State Street	22,335,376	1.2%	1.3%	4.88%	4.65%	-0.07%	-0.14%	21,425,468	1.2%	1.7%	8.40%	8.17%	19,777,366	1.2%	1.7%	7.38%	7.15%	22.08%	21.29%	-17.85%	-18.59%	4.88%	4.18%	-8.34%
MSCI EAFE (3)				5.13%	5.13%	0.82%	0.82%				6.57%	6.57%				6.92%	6.92%	19.80%	19.80%	-13.83%	-13.83%	5.96%	5.96%	-6.10%
Capital Guardian	30,721,460	1.7%	2.5%	5.58%	5.42%	1.27%	1.22%	29,260,135	1.7%	3.8%	6.09%	5.93%	27,586,983	1.6%	3.8%	7.45%	7.29%	20.35%	19.82%	-11.29%	-11.83%	6.93%	6.40%	-6.44%
LSV	-	0.0%	0.0%	N/A	N/A	N/A	N/A	56,673,814	3.3%	3.8%	6.85%	6.70%	53,051,809	3.2%	3.8%	8.36%	8.21%	N/A	N/A	-15.65%	-16.14%	4.91%	4.41%	-9.09%
MSCI EAFE (4)				5.13%	5.13%	0.82%	0.82%				6.57%	6.57%				6.92%	6.92%	19.80%	19.80%	-13.83%	-13.83%	4.92%	4.92%	-6.49%
Clifton	96,452,982	5.4%	5.4%	3.88%	3.85%	0.75%	0.74%	93,279,646	5.4%	2.4%	6.79%	6.76%	87,282,832	5.2%	2.4%	6.10%	6.07%	17.69%	17.60%	-15.37%	-15.46%	N/A	N/A	N/A
MSCI EAFE				5.13%	5.13%	0.82%	0.82%				6.57%	6.57%				6.92%	6.92%	19.80%	19.80%	-13.83%	-13.83%			

ND TEACHERS FUND FOR RETIREMENT
INVESTMENT PERFORMANCE REPORT AS OF MARCH 31, 2013

	March-13							December-12					September-12					Current Fiscal YTD		Prior FY12		3 Years Ended 6/30/2012		5 Years Ended 6/30/2012
		Allocation		Quarter		Month			Allocation		Quarter			Allocation		Quarter								
	Market Value	Actual	Policy	Gross (8)	Net	Gross (8)	Net	Market Value	Actual	Policy	Gross (8)	Net	Market Value	Actual	Policy	Gross (8)	Net	Gross (7)	Net	Gross (7)	Net	Gross	Net	Net
DFA	28,718,015	1.6%	1.3%	8.08%	7.86%	2.09%	2.02%	26,729,855	1.6%	1.7%	8.89%	8.67%	24,562,387	1.5%	1.7%	8.38%	8.16%	27.56%	26.77%	-17.09%	-17.81%	7.91%	7.22%	N/A
Wellington	31,813,249	1.8%	1.3%	7.94%	7.68%	2.50%	2.42%	29,663,333	1.7%	1.7%	5.20%	4.95%	28,227,279	1.7%	1.7%	7.56%	7.31%	22.14%	21.27%	-7.52%	-8.42%	13.15%	12.25%	-2.98%
S&P/Citigroup BMI EPAC < $2BN				***8.51%***	***8.51%***	***2.08%***	***2.08%***				***5.28%***	***5.28%***				***6.96%***	***6.96%***	***22.20%***	***22.20%***	***-15.07%***	***-15.07%***	***7.45%***	***7.45%***	***-6.11%***
Total Developed International	**210,041,082**	**11.7%**	**11.8%**	**5.22%**	**5.09%**	**1.18%**	**1.14%**	**257,032,250**	**14.9%**	**15.0%**	**6.88%**	**6.75%**	**240,488,656**	**14.3%**	**15.0%**	**7.25%**	**7.12%**	**20.62%**	**20.17%**	**-14.72%**	**-15.15%**	**8.42%**	**7.93%**	**-6.05%**
MSCI EAFE (4)				***5.13%***	***5.13%***	***0.82%***	***0.82%***				***6.57%***	***6.57%***				***6.92%***	***6.92%***	***19.80%***	***19.80%***	***-13.83%***	***-13.83%***	***4.92%***	***4.92%***	***-6.49%***
Emerging Markets																								
JP Morgan	10,065,144	0.6%	0.5%	-0.44%	-0.65%	-0.61%	-0.68%	16,449,893	1.0%	0.6%	6.63%	6.42%	15,960,447	0.9%	0.6%	6.49%	6.28%	13.05%	12.38%	-12.96%	-13.67%	10.63%	9.87%	0.43%
PanAgora	6,800,524	0.4%	0.5%	0.27%	0.03%	-0.61%	-0.69%	6,753,313	0.4%	0.6%	4.36%	4.12%	6,682,088	0.4%	0.6%	8.11%	7.86%	13.13%	12.34%	-14.67%	-15.49%	9.90%	9.15%	-1.25%
UBS	9,467,495	0.5%	0.8%	-3.51%	-3.73%	-2.52%	-2.59%	16,228,119	0.9%	1.1%	4.16%	3.93%	16,088,098	1.0%	1.1%	7.66%	7.42%	8.20%	7.49%	-15.06%	-15.82%	11.31%	10.48%	-0.03%
NTGI	7,625,172	0.4%	0.5%	-1.80%	-1.80%	-1.75%	-1.75%	7,732,088	0.4%	0.6%	5.75%	5.75%	7,550,007	0.4%	0.6%	5.15%	5.15%	9.19%	9.19%					
DFA	13,882,200	0.8%	0.5%	2.56%	2.32%	-0.42%	-0.50%	13,499,523	0.8%	0.7%	7.73%	7.47%	12,960,845	0.8%	0.7%	7.40%	7.15%	18.67%	17.82%	-16.19%	-17.02%	15.04%	14.26%	1.06%
Total Emerging Markets	**47,840,535**	**2.7%**	**2.8%**	**-0.62%**	**-0.81%**	**-1.12%**	**-1.19%**	**60,662,935**	**3.5%**	**3.5%**	**5.83%**	**5.63%**	**59,241,486**	**3.5%**	**3.5%**	**7.09%**	**6.88%**	**12.63%**	**11.97%**	**-9.21%**	**-9.98%**	**12.70%**	**12.00%**	**0.96%**
MSCI Emerging Markets				***-1.62%***	***-1.62%***	***-1.72%***	***-1.72%***				***5.58%***	***5.58%***				***7.74%***	***7.74%***	***11.91%***	***11.91%***	***-15.95%***	***-15.95%***	***9.98%***	***9.98%***	***0.14%***
Private Equity																								
Brinson IVCF III	40,180	0.0%		0.00%	0.00%	0.00%	0.00%	40,180	0.0%		-0.24%	-0.24%	40,278	0.0%		0.00%	0.00%	-0.24%	-0.24%	9.19%	9.19%	19.22%	19.22%	14.97%
Coral Partners V	1,429	0.0%		0.00%	0.00%	0.00%	0.00%	1,429	0.0%		0.00%	0.00%	1,487	0.0%		0.00%	0.00%	0.00%	0.00%	12.85%	12.85%	75.73%	75.73%	38.62%
Coral Partners V - Supplemental	92,044	0.0%		0.00%	0.00%	0.00%	0.00%	92,044	0.0%		0.00%	0.00%	95,761	0.0%		0.00%	0.00%	0.00%	0.00%	-58.37%	-58.37%	-15.87%	-15.87%	-14.90%
Coral Momentum Fund (Formerly Fund VI)	1,213,638	0.1%		4.99%	4.99%	0.00%	0.00%	2,054,608	0.1%		1.99%	1.99%	2,095,983	0.1%		-5.18%	-5.18%	1.54%	1.54%	4.47%	4.47%	-14.90%	-14.90%	-16.04%
Brinson 1998 Partnership Fund	54,822	0.0%		0.87%	0.87%	0.87%	0.87%	54,349	0.0%		3.83%	3.83%	54,460	0.0%		1.44%	1.44%	6.24%	6.24%	-14.46%	-14.46%	-1.43%	-1.43%	-7.20%
Brinson 1999 Partnership Fund	517,872	0.0%		0.20%	0.20%	0.20%	0.20%	516,856	0.0%		2.49%	2.49%	524,650	0.0%		3.42%	3.42%	6.21%	6.21%	-5.66%	-5.66%	8.72%	8.72%	0.81%
Brinson 2000 Partnership Fund	1,640,910	0.1%		-1.19%	-1.19%	-1.19%	-1.19%	1,660,697	0.1%		1.97%	1.97%	1,931,983	0.1%		2.43%	2.43%	3.20%	3.20%	6.74%	6.74%	14.10%	14.10%	5.38%
Brinson 2001 Partnership Fund	1,895,948	0.1%		0.90%	0.90%	0.90%	0.90%	2,065,828	0.1%		4.94%	4.94%	2,199,468	0.1%		-0.22%	-0.22%	5.66%	5.66%	4.90%	4.90%	12.44%	12.44%	2.58%
Brinson 2002 Partnership Fund	1,112,198	0.1%		-1.36%	-1.36%	-1.36%	-1.36%	1,127,503	0.1%		2.98%	2.98%	1,309,434	0.1%		-0.29%	-0.29%	1.29%	1.29%	12.41%	12.41%	22.51%	22.51%	3.79%
Brinson 2003 Partnership Fund	383,385	0.0%		1.33%	1.33%	1.33%	1.33%	378,345	0.0%		2.61%	2.61%	416,104	0.0%		-0.58%	-0.58%	3.38%	3.38%	-5.78%	-5.78%	10.46%	10.46%	-0.59%
Total Brinson Partnership Funds	5,605,136	0.3%		-0.21%	-0.21%	-0.21%	-0.21%	5,803,578	0.3%		3.25%	3.25%	6,436,099	0.4%		0.88%	0.88%	3.95%	3.95%	4.35%	4.35%	13.60%	13.60%	3.89%
Brinson 1999 Non-US Partnership Fund	239,917	0.0%		12.63%	12.63%	12.63%	12.63%	213,011	0.0%		2.46%	2.46%	216,285	0.0%		9.24%	9.24%	26.07%	26.07%	-0.36%	-0.36%	18.50%	18.50%	2.79%
Brinson 2000 Non-US Partnership Fund	517,306	0.0%		-0.45%	-0.45%	-0.45%	-0.45%	519,634	0.0%		-0.45%	-0.45%	622,195	0.0%		0.04%	0.04%	-0.86%	-0.86%	-3.49%	-3.49%	12.53%	12.53%	2.59%
Brinson 2001 Non-US Partnership Fund	342,166	0.0%		-0.69%	-0.69%	-0.69%	-0.69%	344,526	0.0%		8.52%	8.52%	384,710	0.0%		-3.59%	-3.59%	3.90%	3.90%	-14.12%	-14.12%	5.11%	5.11%	-7.15%
Brinson 2002 Non-US Partnership Fund	1,283,448	0.1%		2.31%	2.31%	2.31%	2.31%	1,366,133	0.1%		4.43%	4.43%	1,434,234	0.1%		2.74%	2.74%	9.76%	9.76%	-2.78%	-2.78%	12.99%	12.99%	-1.62%
Brinson 2003 Non-US Partnership Fund	900,900	0.1%		12.39%	12.39%	12.39%	12.39%	876,862	0.1%		7.51%	7.51%	848,524	0.1%		9.23%	9.23%	31.99%	31.99%	-11.60%	-11.60%	16.11%	16.11%	4.71%
Brinson 2004 Non-US Partnership Fund	606,003	0.0%		3.70%	3.70%	3.70%	3.70%	613,191	0.0%		1.26%	1.26%	629,998	0.0%		1.53%	1.53%	6.61%	6.61%	-8.24%	-8.24%	9.51%	9.51%	0.91%
Total Brinson Non-US Partnership Fund	3,889,739	0.2%		4.63%	4.63%	4.63%	4.63%	3,933,357	0.2%		4.15%	4.15%	4,135,946	0.2%		3.21%	3.21%	12.47%	12.47%	-6.71%	-6.71%	12.87%	12.87%	0.73%
Adams Street 2008 Non-US Partnership Fd	2,026,863	0.1%		3.19%	3.19%	3.19%	3.19%	1,964,221	0.1%		1.73%	1.73%	1,904,878	0.1%		3.75%	3.75%	8.91%	8.91%	-1.84%	-1.84%	3.99%	3.99%	N/A
Brinson BVCF IV	2,067,571	0.1%		18.51%	18.51%	0.00%	0.00%	1,744,589	0.1%		-3.65%	-3.65%	1,883,774	0.1%		0.00%	0.00%	14.19%	14.19%	64.19%	64.19%	89.31%	89.31%	44.31%
Adams Street Direct Co-investment Fund	7,783,595	0.4%		3.79%	3.79%	0.00%	0.00%	7,924,163	0.5%		-1.87%	-1.87%	8,869,298	0.5%		0.00%	0.00%	1.85%	1.85%	5.82%	5.82%	14.37%	14.37%	1.24%
Adams Street 2010 Direct Fund	395,633	0.0%		3.21%	3.21%	3.21%	3.21%	355,674	0.0%		-0.86%	-0.86%	348,088	0.0%		0.00%	0.00%	2.32%	2.32%	22.19%	22.19%	N/A	N/A	N/A
Adams Street 2010 Non-US Emerging Mkts	136,895	0.0%		-1.12%	-1.12%	-1.12%	-1.12%	124,499	0.0%		-1.61%	-1.61%	109,865	0.0%		-0.62%	-0.62%	-3.32%	-3.32%	-21.77%	-21.77%	N/A	N/A	N/A
Adams Street 2010 Non-US Developed Mkts	561,271	0.0%		2.82%	2.82%	2.82%	2.82%	530,315	0.0%		4.05%	4.05%	487,997	0.0%		3.38%	3.38%	10.61%	10.61%	4.57%	4.57%	N/A	N/A	N/A
Adams Street 2010 Partnership Fund	1,211,123	0.1%		1.85%	1.85%	1.85%	1.85%	1,189,102	0.1%		3.47%	3.47%	1,106,337	0.1%		1.41%	1.41%	6.88%	6.88%	8.84%	8.84%	N/A	N/A	N/A
Total Adams Street 2010 Funds	2,304,922	0.1%		2.16%	2.16%	2.16%	2.16%	2,199,590	0.1%		2.60%	2.60%	2,052,288	0.1%		1.52%	1.52%	6.40%	6.40%	8.71%	8.71%	N/A	N/A	N/A
Matlin Patterson Global Opportunities	5,523	0.0%		-6.26%	-6.26%	-6.26%	-6.26%	5,891	0.0%		1.64%	1.64%	6,031	0.0%		24.07%	24.07%	18.21%	18.21%	-21.48%	-21.48%	58.17%	58.17%	-0.76%
Matlin Patterson Global Opportunities II	766,358	0.0%		-1.26%	-1.26%	-1.26%	-1.26%	776,169	0.0%		0.02%	0.02%	807,371	0.0%		0.00%	0.00%	-1.25%	-1.25%	-79.03%	-79.03%	-53.26%	-53.26%	-45.01%
Matlin Patterson Global Opportunities III	12,805,167	0.7%		12.96%	12.96%	12.96%	12.96%	11,336,141	0.7%		10.22%	10.22%	11,199,258	0.7%		0.00%	0.00%	24.51%	24.51%	124.86%	124.86%	44.50%	44.50%	5.42%
InvestAmerica (Lewis and Clark Fund)	2,914,287	0.2%		9.58%	9.58%	0.00%	0.00%	2,659,637	0.2%		0.00%	0.00%	3,284,605	0.2%		0.00%	0.00%	9.58%	9.58%	6.13%	6.13%	8.60%	8.60%	7.72%
L&C II	4,320,034	0.2%		-5.85%	-5.85%	0.00%	0.00%	3,973,060	0.2%		0.00%	0.00%	4,017,598	0.2%		0.00%	0.00%	-5.85%	-5.85%	-3.26%	-3.26%	-10.62%	N/A	N/A
Corsair III (2)	5,319,529	0.3%		-3.41%	-3.41%	-2.87%	-2.87%	5,488,830	0.3%		-6.23%	-6.23%	5,980,998	0.4%		-0.60%	-0.60%	-9.97%	-9.97%	-1.10%	-2.14%	1.97%	1.61%	5.38%
Corsair III - ND Investors LLC (2)	4,820,282	0.3%		-1.82%	-1.82%	-1.36%	-1.36%	4,886,595	0.3%		-0.47%	-0.47%	5,083,961	0.3%		0.00%	0.00%	-2.28%	-2.28%	5.30%	5.04%	1.15%	1.06%	N/A
Corsair IV	4,180,842	0.2%		-0.22%	-0.22%	0.50%	0.50%	4,451,879	0.3%		-1.74%	-1.74%	4,843,042	0.3%		-1.20%	-1.20%	-3.14%	-3.14%	-15.55%	-16.03%	N/A	N/A	N/A
Capital International (CIPEF V)	10,505,237	0.6%		-11.90%	-11.90%	-11.47%	-11.47%	11,896,058	0.7%		-0.55%	-0.55%	11,631,956	0.7%		-0.47%	-0.47%	-12.79%	-12.79%	-4.74%	-4.74%	13.64%	13.57%	N/A
Capital International (CIPEF VI)	2,491,452	0.1%		-1.87%	-1.87%	0.61%	0.61%	3,023,081	0.2%		-4.12%	-4.12%	2,367,140	0.1%		-2.95%	-2.95%	-8.69%	-8.69%	N/A	N/A	N/A	N/A	N/A
EIG (formerly TCW)	13,794,910	0.8%		-2.23%	-2.23%	-0.63%	-0.63%	15,809,140	0.9%		-0.33%	-0.33%	16,744,602	1.0%		0.42%	0.42%	-2.13%	-2.13%	7.17%	7.17%	13.10%	13.10%	11.58%
Quantum Resources	4,092,554	0.2%		0.00%	0.00%	0.00%	0.00%	4,698,490	0.3%		4.33%	4.33%	5,351,643	0.3%		21.08%	21.08%	26.32%	26.32%	-0.85%	-0.85%	-13.12%	-13.12%	-49.44%
Quantum Energy Partners	3,778,538	0.2%		0.00%	0.00%	0.00%	0.00%	4,326,334	0.3%		8.29%	8.29%	4,235,403	0.3%		-2.37%	-2.37%	5.73%	5.73%	30.29%	30.29%	16.80%	16.80%	3.54%
Total Private Equity (8)	**94,819,832**	**5.3%**	**5.0%**	**0.36%**	**0.36%**	**0.10%**	**0.10%**	**99,089,065**	**5.8%**	**5.0%**	**1.27%**	**1.27%**	**103,072,192**	**6.1%**	**5.0%**	**0.88%**	**0.88%**	**2.53%**	**2.53%**	**5.12%**	**5.12%**	**12.90%**	**12.90%**	**-0.14%**

ND TEACHERS FUND FOR RETIREMENT
INVESTMENT PERFORMANCE REPORT AS OF MARCH 31, 2013

	March-13							December-12					September-12					Current Fiscal YTD		Prior FY12		3 Years Ended 6/30/2012		5 Years Ended 6/30/2012
		Allocation		Quarter		Month			Allocation		Quarter			Allocation		Quarter								
	Market Value	Actual	Policy	Gross (8)	Net	Gross (8)	Net	Market Value	Actual	Policy	Gross (8)	Net	Market Value	Actual	Policy	Gross (8)	Net	Gross (7)	Net	Gross (7)	Net	Gross	Net	Net
GLOBAL FIXED INCOME	384,849,003	21.5%	22.0%	0.98%	0.91%	0.45%	0.43%	382,688,047	22.2%	22.0%	2.89%	2.82%	375,572,494	22.3%	22.0%	4.19%	4.13%	8.24%	8.04%					
Benchmark				-0.22%	-0.22%	0.16%	0.16%				0.62%	0.62%				2.88%	2.88%	3.30%	3.30%					
Domestic Fixed Income	295,630,580	16.5%	17.0%	1.90%	1.84%	0.59%	0.57%	291,600,781	16.9%	17.0%	3.42%	3.36%	286,690,303	17.0%	17.0%	3.91%	3.86%	9.50%	9.32%					
Benchmark				0.76%	0.76%	0.36%	0.36%				1.11%	1.11%				2.44%	2.44%	4.37%	4.37%					
Investment Grade Fixed Income																								
PIMCO (DiSCO II) (8)	41,965,230	2.3%	1.9%	4.97%	4.97%	0.59%	0.59%	40,140,981	2.3%	1.9%	14.74%	14.74%	34,973,450	2.1%	1.9%	9.64%	9.64%	32.05%	32.05%	N/A	N/A	N/A	N/A	N/A
BC Aggregate				-0.12%	-0.12%	0.08%	0.08%				0.21%	0.21%				1.58%	1.58%	1.68%	1.68%	7.47%	7.47%	6.93%	6.93%	6.79%
Bank of ND	19,182,179	1.1%	1.2%	-2.35%	-2.37%	-0.11%	-0.12%	19,727,199	1.1%	1.2%	-0.63%	-0.64%	19,848,156	1.2%	1.2%	-1.20%	-1.21%	-4.13%	-4.17%	9.53%	9.47%	7.95%	7.89%	7.73%
BC Long Treasuries				-2.38%	-2.38%	-0.10%	-0.10%				-0.77%	-0.77%				0.20%	0.20%	-2.94%	-2.94%	15.86%	15.86%	9.62%	9.62%	8.26%
PIMCO (Unconstrained)	24,576,290	1.4%	1.4%	0.84%	0.84%	-0.09%	-0.09%	24,471,302	1.4%	1.4%	0.76%	0.76%	28,336,708	1.7%	1.4%	2.65%	2.65%	4.30%	4.30%	N/A	N/A	N/A	N/A	N/A
3m LIBOR				0.08%	0.08%	0.03%	0.03%				0.08%	0.08%				0.11%	0.11%	0.27%	0.27%					
Declaration (Total Return)	24,275,421	1.4%	1.4%	2.60%	2.45%	0.61%	0.56%	23,756,419	1.4%	1.4%	2.92%	2.76%	23,075,219	1.4%	1.4%	3.49%	3.34%	9.28%	8.79%	N/A	N/A	N/A	N/A	N/A
3m LIBOR				0.08%	0.08%	0.03%	0.03%				0.08%	0.08%				0.11%	0.11%	0.27%	0.27%					
Western Asset	40,818,070	2.3%	2.4%	-0.08%	-0.13%	0.11%	0.09%	41,036,466	2.4%	2.4%	-0.24%	-0.28%	41,139,291	2.4%	2.4%	1.33%	1.29%	1.01%	0.87%	N/A	N/A	N/A	N/A	N/A
PIMCO (MBS)	60,343,501	3.4%	3.6%	-0.27%	-0.29%	0.00%	-0.01%	60,778,912	3.5%	3.6%	-0.04%	-0.07%	60,810,157	3.6%	3.6%	2.05%	2.02%	1.73%	1.66%	N/A	N/A	N/A	N/A	N/A
BC Mortgage Backed Securities Index				-0.05%	-0.05%	0.12%	0.12%				-0.20%	-0.20%				1.13%	1.13%	0.88%	0.88%					
Total Investment Grade Fixed Income	211,160,692	11.8%	12.0%	1.03%	0.99%	0.19%	0.17%	209,911,279	12.2%	12.0%	2.82%	2.78%	208,182,981	12.4%	12.0%	3.02%	2.99%	7.02%	6.91%	6.24%	6.01%	6.53%	5.91%	4.55%
BC Aggregate				-0.12%	-0.12%	0.08%	0.08%				0.21%	0.21%				1.58%	1.58%	1.68%	1.68%	7.47%	7.47%	6.93%	6.93%	6.79%
Below Investment Grade Fixed Income																								
Loomis Sayles	78,422,009	4.4%	4.7%	4.17%	4.05%	1.36%	1.32%	75,155,791	4.4%	4.6%	4.41%	4.29%	72,288,176	4.3%	4.6%	6.38%	6.25%	15.71%	15.29%	2.57%	2.07%	16.71%	16.20%	6.96%
Goldman Sachs 2006 Fund (8)	1,893,127	0.1%	0.1%	7.32%	7.32%	8.48%	8.48%	1,854,931	0.1%	0.1%	2.92%	2.92%	1,842,965	0.1%	0.1%	0.37%	0.37%	10.86%	10.86%	-20.28%	-20.28%	31.00%	31.00%	-2.25%
Goldman Sachs Fund V (8)	4,153,271	0.2%	0.2%	2.26%	2.26%	3.51%	3.51%	4,678,780	0.3%	0.3%	6.04%	6.04%	4,376,180	0.3%	0.3%	-1.00%	-1.00%	7.36%	7.36%	7.04%	7.04%	22.19%	22.19%	N/A
PIMCO (8)	1,482	0.0%	0.0%	N/A	N/A	N/A	N/A	0	0.0%	0.0%	N/A	N/A	0	0.0%	0.0%	386.85%	386.85%	N/A	N/A	5.54%	5.54%	30.43%	30.43%	N/A
Total Below Investment Grade Fixed Income	84,469,889	4.7%	5.0%	4.13%	4.01%	1.62%	1.58%	81,689,502	4.7%	5.0%	4.98%	4.86%	78,507,322	4.7%	5.0%	6.33%	6.22%	16.24%	15.86%	3.45%	3.06%	17.33%	16.95%	3.99%
LB High Yield 2% Issuer Constrained Index				2.89%	2.89%	1.02%	1.02%				3.29%	3.29%				4.53%	4.53%	11.09%	11.09%	7.21%	7.21%	16.20%	16.20%	8.62%
International Fixed Income	89,218,423	5.0%	5.0%	-1.96%	-2.04%	-0.01%	-0.04%	91,087,266	5.3%	5.0%	1.20%	1.11%	88,882,192	5.3%	5.0%	5.11%	5.02%	4.29%	4.02%					
Benchmark				-3.51%	-3.51%	-0.50%	-0.50%				-1.03%	-1.03%				4.37%	4.37%	-0.33%	-0.33%					
Developed Investment Grade Int'l FI																								
UBS Global (Brinson)	42,144,160	2.3%	2.5%	-3.93%	-4.00%	-0.49%	-0.52%	43,903,978	2.6%	2.5%	-0.84%	-0.92%	43,731,242	2.6%	2.5%	4.77%	4.69%	-0.20%	-0.42%	-0.87%	-1.16%	5.36%	5.05%	6.72%
BC Global Aggregate ex-US (6)				-3.51%	-3.51%	-0.50%	-0.50%				-1.03%	-1.03%				4.37%	4.37%	-0.33%	-0.33%	-0.64%	-0.64%	5.23%	5.23%	7.45%
Brandywine	47,074,263	2.6%	2.5%	-0.12%	-0.22%	0.42%	0.39%	47,183,288	2.7%	2.5%	3.17%	3.07%	45,150,950	2.7%	2.5%	5.45%	5.35%	8.66%	8.35%	9.67%	9.25%	13.36%	12.95%	9.36%
BC Global Aggregate (ex-US)				-2.10%	-2.10%	-0.25%	-0.25%				-0.48%	-0.48%				3.27%	3.27%	0.62%	0.62%	2.73%	2.73%	6.31%	6.31%	7.11%
Total Developed Investment Grade Int'l FI	89,218,423	5.0%	5.0%	-1.96%	-2.04%	-0.01%	-0.04%	91,087,266	5.3%	5.0%	1.20%	1.11%	88,882,192	5.3%	5.0%	5.11%	5.02%	4.29%	4.02%	4.61%	4.25%	9.76%	9.40%	8.29%
BC Global Aggregate ex-US				-3.51%	-3.51%	-0.50%	-0.50%				-1.03%	-1.03%				4.37%	4.37%	-0.33%	-0.33%	-0.64%	-0.64%	5.23%	5.23%	7.45%

ND TEACHERS FUND FOR RETIREMENT
INVESTMENT PERFORMANCE REPORT AS OF MARCH 31, 2013

	March-13							December-12					September-12					Current Fiscal YTD		Prior FY12		3 Years Ended 6/30/2012		5 Years Ended 6/30/2012
		Allocation		Quarter		Month			Allocation		Quarter			Allocation		Quarter								
	Market Value	Actual	Policy	Gross (8)	Net	Gross (8)	Net	Market Value	Actual	Policy	Gross (8)	Net	Market Value	Actual	Policy	Gross (8)	Net	Gross (7)	Net	Gross (7)	Net	Gross	Net	Net
GLOBAL REAL ASSETS	***329,632,534***	***18.4%***	***20.0%***	***0.74%***	***0.64%***	***0.62%***	***0.59%***	***325,523,640***	***18.9%***	***20.0%***	***3.28%***	***3.17%***	***322,866,740***	***19.2%***	***20.0%***	***1.36%***	***1.26%***	***5.45%***	***5.14%***					
Benchmark				***3.13%***	***3.13%***	***0.98%***	***0.98%***				***2.48%***	***2.48%***				***1.59%***	***1.59%***	***7.38%***	***7.38%***					
Global Real Estate																								
INVESCO - Core	62,589,602			5.44%	5.34%	3.25%	3.22%	59,551,703			-0.10%	-0.20%	60,772,364			2.80%	2.70%	8.28%	7.96%	8.97%	8.54%	8.03%	7.54%	-1.28%
INVESCO - Fund II (8)	17,210,405			-1.52%	-1.52%	0.00%	0.00%	20,752,901			9.32%	9.32%	19,782,387			0.00%	0.00%	7.66%	7.66%	28.70%	28.70%	-3.10%	-3.10%	N/A
INVESCO - Fund III (9)	9,236,118			-1.56%	-1.56%	0.00%	0.00%	9,394,137			4.34%	4.34%	9,178,937			0.00%	0.00%	2.71%	2.71%	N/A	N/A	N/A	N/A	N/A
INVESCO - Asia Real Estate Fund (8)	10,711,024			-8.18%	-8.18%	-1.87%	-1.87%	8,814,404			8.07%	8.07%	8,315,072			-3.39%	-3.39%	-4.14%	-4.14%	1.09%	1.09%	-22.90%	-22.90%	N/A
J.P. Morgan Strategic & Special Funds	56,646,606			3.57%	3.35%	1.21%	1.14%	54,887,648			2.74%	2.52%	54,593,439			3.65%	3.43%	10.29%	9.59%	13.33%	12.37%	8.42%	7.42%	-2.25%
J.P. Morgan Alternative Property Fund	2,802,964			9.73%	9.66%	4.97%	4.94%	2,684,553			7.61%	7.54%	7,794,835			3.11%	3.04%	21.75%	21.51%	27.71%	27.38%	2.93%	2.15%	-9.30%
J.P. Morgan Greater Europe Fund (8)	1,767,351			-7.71%	-7.71%	-6.92%	-6.92%	1,929,444			-23.63%	-23.63%	3,127,503			-16.43%	-16.43%	-41.10%	-41.10%	-100.01%	-100.01%	N/A	N/A	N/A
J.P. Morgan Greater China Property Fund (8)	10,081,641			-2.66%	-2.66%	-2.66%	-2.66%	10,369,607			1.73%	1.73%	10,691,423			-4.30%	-4.30%	-5.22%	-5.22%	-4.20%	-4.20%	3.62%	3.62%	N/A
Total Global Real Estate	**171,045,710**	**9.5%**	**10.0%**	**2.30%**	**2.19%**	**1.32%**	**1.28%**	**168,384,396**	**9.8%**	**10.0%**	**2.57%**	**2.45%**	**174,255,960**	**10.4%**	**10.0%**	**1.42%**	**1.32%**	**6.43%**	**6.08%**	**12.97%**	**12.46%**	**7.34%**	**6.72%**	**-2.97%**
NCREIF TOTAL INDEX				***2.57%***	***2.57%***	***0.85%***	***0.85%***				***2.54%***	***2.54%***				***2.34%***	***2.34%***	***7.63%***	***7.63%***	***12.04%***	***12.04%***	***8.82%***	***8.82%***	***2.51%***
Timber																								
TIR - Teredo (7)	34,417,435	1.9%		-5.49%	-5.49%	0.00%	0.00%	36,416,561	2.1%		6.97%	6.97%	32,948,859	2.0%		0.00%	0.00%	1.10%	1.10%	-2.76%	-2.76%	4.79%	4.79%	8.28%
TIR - Springbank	55,780,150	3.1%		-1.78%	-1.78%	0.00%	0.00%	56,805,785	3.3%		0.19%	0.19%	54,886,635	3.3%		0.02%	0.02%	-1.58%	-1.58%	-5.48%	-5.48%	-8.06%	-8.06%	-1.70%
Total Timber	**90,197,584**	**5.0%**	**5.0%**	**-3.23%**	**-3.23%**	**0.00%**	**0.00%**	**93,222,345**	**5.4%**	**5.0%**	**2.73%**	**2.73%**	**87,835,494**	**5.2%**	**5.0%**	**0.01%**	**0.01%**	**-0.58%**	**-0.58%**					
NCREIF Timberland Index(8)				***5.92%***	***5.92%***	***1.94%***	***1.94%***				***5.92%***	***5.92%***				***0.75%***	***0.75%***	***13.03%***	***13.03%***	***1.49%***	***1.49%***	***-3.83%***	***-0.56%***	***4.43%***
Infrastructure																								
JP Morgan (Asian)	11,653,916	0.6%		-1.65%	-1.65%	-1.78%	-1.78%	8,971,625	0.5%		21.99%	21.99%	7,491,263	0.4%		0.00%	0.00%	*19.98%*	19.98%	*-4.29%*	-4.29%	-0.51%	-0.68%	N/A
JP Morgan (IIF)	44,678,623	2.5%		4.03%	3.71%	0.00%	-0.11%	43,058,330	2.5%		4.42%	4.09%	42,053,403	2.5%		4.61%	4.28%	13.64%	12.56%	4.51%	3.22%	5.87%	4.40%	-0.91%
Credit Suisse	12,056,701	0.7%		-0.28%	-0.28%	0.00%	0.00%	11,886,945	0.7%		1.77%	1.77%	11,230,619	0.7%		-0.31%	-0.31%	1.17%	1.17%	N/A	N/A	N/A	N/A	N/A
Total Infrastructure (8)	**68,389,239**	**3.8%**	**5.0%**	**2.39%**	**2.17%**	**-0.29%**	**-0.36%**	**63,916,900**	**3.7%**	**5.0%**	**6.02%**	**5.79%**	**60,775,286**	**3.6%**	**5.0%**	**3.09%**	**2.86%**	**11.90%**	**11.18%**					
CPI				***1.52%***	***1.52%***	***0.28%***	***0.28%***				***-1.01%***	***-1.01%***				***0.95%***	***0.95%***	***1.45%***	***1.45%***					
Cash Equivalents																								
Northern Trust STIF	24,645,129			0.03%	0.03%	0.01%	0.01%	21,745,167			0.03%	0.03%	8,753,017			0.03%	0.03%	0.08%	0.08%	0.13%	0.13%	0.14%	0.14%	0.42%
Total Cash Equivalents	**24,645,129**	**1.4%**	**1.0%**	**0.03%**	**0.03%**	**0.01%**	**0.01%**	**21,745,167**	**1.3%**	**1.0%**	**0.03%**	**0.03%**	**8,753,017**	**0.5%**	**1.0%**	**0.03%**	**0.03%**	**0.08%**	**0.08%**	**0.13%**	**0.13%**	**0.19%**	**0.19%**	**0.46%**
90 Day T-Bill				***0.02%***	***0.02%***	***0.02%***	***0.02%***				***0.04%***	***0.04%***				***0.03%***	***0.03%***	***0.09%***	***0.09%***	***0.06%***	***0.06%***	***0.13%***	***0.13%***	***0.99%***

NOTE: Monthly returns and market values are preliminary and subject to change.
New asset class structure began October 1, 2011. Composite returns for new composites not available prior to that date.
Portfolios moved between asset classes will show historical returns in new position.

(1) Epoch was included in the Large Cap Domestic Equity composite through 12/31/11.
(2) Prior to January 1, 2012, the benchmark was S&P 500.
(3) This benchmark was changed to the MSCI EAFE (unhedged) as of December 1, 2004.
(4) This benchmark was changed to the MSCI EAFE (unhedged) as of April 1, 2011.
(5) Prior to January 1, 2005, the benchmark was the First Boston Convertible Index.
(6) Prior to December 1, 2009, the benchmark was the Citigroup World Gov't Bond Index ex-US
(7) Prior to June 1, 2006, the Teredo properties were under the management of RMK.
(8) All limited partnership-type investments' returns will only be reported net of fees, which is standard practice by the investment consultant.

ND STATE INVESTMENT BOARD MEETING

Friday, May 17, 2013, 8:30 a.m.
State Capitol, Peace Garden Room
Bismarck, ND

AGENDA

I. CALL TO ORDER AND ACCEPTANCE OF AGENDA

II. ACCEPTANCE OF MINUTES (April 26, 2013)

III. INVESTMENTS

A. Calamos (90 min) (to follow)
B. Pension and Insurance Trust's Performance Measurement - (enclosed) Mr. Erlendson (45 min)
C. Bank of ND Update - Ms. Flanagan (10 min)

IV. GOVERNANCE

A. Administration
   1. Search Committee Update - Search Committee
   2. Compensation Committee (to follow)

V. MONITORING REPORTS (acceptance needed - questions only) (5 min)

1. Watch List - (enclosed) Mr. Schulz

VI. OTHER

Next SIB Meeting - June 28, 2013, 8:30 a.m. - State Capitol, Peace Garden Room
SIB Audit Committee meeting - May 17, 2013, 1:00 p.m. - State Capitol, Peace Garden Room

VII. ADJOURNMENT

NORTH DAKOTA STATE INVESTMENT BOARD
MINUTES OF THE
APRIL 26, 2013, BOARD MEETING

BOARD MEMBERS PRESENT:
Drew Wrigley, Lt. Governor, Chair
Mike Sandal, Vice Chair
Clarence Corneil, TFFR Board
Levi Erdmann, PERS Board
Lance Gaebe, Land Commissioner
Mike Gessner, TFFR Board
Adam Hamm, Insurance Commissioner
Howard Sage, PERS Board
Kelly Schmidt, State Treasurer
Cindy Ternes, Workforce Safety & Insurance
Bob Toso, TFFR Board

STAFF PRESENT:
Connie Flanagan, Fiscal & Investment Officer
Bonnie Heit, Office Manager
Fay Kopp, Interim Executive Director
Leslie Moszer, Compliance Officer
Darren Schulz, Interim CIO
Susan Walcker, Investment Accountant

OTHERS PRESENT:
Weldee Baetsch, former PERS & SIB Trustee
Chanakya Chakravarti, JP Morgan
Hrushikesh Kar, JP Morgan
Jan Murtha, Attorney General’s Office
George Ochs, JP Morgan
Jim Sakelaris, JP Morgan
Dave Thompson, Prairie Public

CALL TO ORDER:

Lt. Governor Wrigley called the State Investment Board (SIB) meeting to order at 8:30 a.m. on Friday, April 26, 2013, at Workforce Safety & Insurance, 1600 E Century, Bismarck, ND.

A quorum was present for the purpose of conducting business.

AGENDA:

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. CORNEIL AND CARRIED ON A VOICE VOTE TO ACCEPT THE APRIL 26, 2013, AGENDA.

AYES: COMMISSIONER GAEBE, TREASURER SCHMIDT, MR. SANDAL, MR. CORNEIL, MS. TERNES, MR. GESSNER, MR. ERDMANN, MR. TOSO, MR. SAGE, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED
ABSENT: COMMISSIONER HAMM

MINUTES:

The minutes were considered from the March 22, 2013, meeting,

IT WAS MOVED BY MR. CORNEIL AND SECONDED BY COMMISSIONER GAEBE AND CARRIED ON A VOICE VOTE TO ACCEPT THE MARCH 22, 2013, MINUTES AS WRITTEN.

AYES: MR. GESSNER, COMMISSIONER GAEBE, MR. SAGE, MS. TERNES, TREASURER SCHMIDT, MR. TOSO, MR. CORNEIL, MR. ERDMANN, MR. SANDAL, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED
ABSENT: COMMISSIONER HAMM

EDUCATION:

JP Morgan representatives presented an educational segment on India real estate. The Board took no action on the subject matter.

INVESTMENTS:

Legacy Fund – Mr. Schulz and Ms. Flanagan attended the Legacy and Budget Stabilization Fund Advisory Board (Advisory Board) meeting on April 2, 2013. R.V. Kuhns & Associates, who were contracted by the SIB at their September 28, 2012, meeting to conduct a comprehensive asset allocation and spending policy analysis on the Legacy Fund, presented their findings. After reviewing their options, the Advisory Board adopted the following asset allocation mix for the Legacy Fund:

Broad US Equity 30%
Broad International Equity 20%
Fixed Income 35%
Core Real Estate 5%
Diversified Real Assets 10%

Mr. Schulz and Ms. Flanagan also attended the Advisory Board's April 25, 2013, meeting. Mr. Schulz, at the request of Advisory Board, presented an educational segment on investment pooling. R.V. Kuhns recommended the Legacy Fund be pooled for cost-savings/efficiencies. The Advisory Board revised their investment policy statement to allow pooling of the Legacy Fund with other SIB funds.

The SIB discussed the revisions to the investment policy statement and after discussion,

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. SANDAL AND CARRIED ON A ROLL CALL VOTE TO ACCEPT THE REVISED INVESTMENT POLICY STATEMENT FOR THE LEGACY FUND.

AYES: MR. CORNEIL, MR. ERDMANN, COMMISSIONER GAEBE, MR. GESSNER, COMMISSIONER HAMM, MR. SAGE, MR. SANDAL, TREASURER SCHMIDT, MS. TERNES, MR. TOSO, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

Mr. Schulz will be working with R.V. Kuhns and Callan Associates to develop a work plan to implement the new asset allocation policy and will report back to the board.

The SIB thanked Mr. Schulz and Ms. Flanagan for working with their client, the Advisory Board, to assist them in implementing an investment plan for the Legacy Fund.

Bank of North Dakota (BND) – Mr. Schulz stated on April 5, 2013, he requested the BND provide information by April 18, 2013, on whether the BND could offer a lower investment management fee and also enhance their current investment process as a result of the discussions that occurred at the March 22, 2013, SIB meeting concerning the two passive fixed income mandates currently managed by the BND.

Lt. Governor Wrigley stated he received a letter on April 25, 2013, from the BND declining to provide its services under terms that are materially different from those it presently offers. BND also proposed the SIB mutually agree to terminate their investment management agreement which has been in effect since July 1, 1989.

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. CORNEIL AND CARRIED ON A ROLL CALL VOTE TO BRING BACK TO THE TABLE THE FOLLOWING MOTION FROM THE MARCH 22, 2013, SIB MEETING,

TREASURER SCHMIDT MOVED AND MR. CORNEIL SECONDED TO TERMINATE BND'S PASSIVE FIXED INCOME MANDATES OF $160 MILLION AND TRANSITION THE ASSETS TO STATE STREET.

AYES: TREASURER SCHMIDT, MR. GESSNER, COMMISSIONER HAMM, MS. TERNES, COMMISSIONER GAEBE, MR. SAGE, MR. TOSO, MR. SANDAL, MR. ERDMANN, MR. CORNEIL, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

Discussion followed on the motion. After discussion,

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. GESSNER TO AMEND THE MOTION THAT IS ON THE TABLE TO MUTUALLY AGREE WITH THE BND TO TERMINATE THEIR RELATIONSHIP OF THE MANAGEMENT OF THE PASSIVE FIXED INCOME MANDATES OF $160 MILLION AND TRANSITION THE ASSETS TO STATE STREET.

Discussion followed,

IT WAS MOVED BY MR. ERDMANN TO CALL THE QUESTION WHICH WAS CARRIED ON A ROLL CALL VOTE.

AYES: MR. SAGE, MR. SANDAL, MR. CORNEIL, MR. GESSNER, MR. TOSO, MR. ERDMANN, MS. TERNES, COMMISSIONER HAMM, COMMISSIONER GAEBE, TREASURER SCHMIDT, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

A roll call vote was then taken on the motion to amend the tabled motion,

AYES: MR. ERDMANN, TREASURER SCHMIDT, MR. CORNEIL, COMMISSIONER GAEBE, MR. TOSO, MR. SANDAL, COMMISSIONER HAMM, MR. GESSNER, MR. SAGE, MS. TERNES, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

A roll call vote was then taken on the following motion,

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. GESSNER THAT THE SIB MUTALLY AGREES WITH THE BND TO TERMINATE THEIR RELATIONSHIP OF THE MANAGEMENT OF THE PASSIVE FIXED INCOME MANDATES OF $160 MILLION AND TRANSITION THE ASSETS TO STATE STREET.

AYES: MS. TERNES, MR. CORNEIL, COMMISSIONER HAMM, TREASURER SCHMIDT, COMMISSIONER GAEBE, MR. ERDMANN, MR. TOSO, MR. SANDAL, MR. SAGE, MR. GESSNER, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

Mr. Schultz reported that Blackrock Solutions, New York, as a professional courtesy, worked with BND and its legal counsel, Mr. Dave Schaibley, Mr. Schulz, Ms. Flanagan, and Ms. Murtha, to conduct an analysis of the losses that occurred as a result of BND's delay in transitioning the assets in the Pension Trust from a Barclays Capital Government Index mandate to a Barclays Capital Long Treasury Index. Blackrock Solutions' analysis concurred with Mr. Schulz's and Ms. Flanagan's analysis that a loss of $2.542 million had occurred. All of the other entities involved concurred with the analysis and BND will expedite the credit based on the loss calculation as soon as possible.

IT WAS MOVED BY MR. SAGE AND SECONDED BY TREASURER SCHMIDT AND CARRIED ON A ROLL CALL VOTE TO REMOVE BND FROM THE WATCH LIST AS THE WATCH LIST DOES NOT PERTAIN TO THE SIB/BND MATCH LOAN PROGRAM RELATIONSHIP OF $120 MILLION.

AYES: COMMISSIONER HAMM, MS. TERNES, MR. CORNEIL, MR. SANDAL, TREASURER SCHMIDT, MR. GESSNER, MR. SAGE, COMMISSIONER GAEBE, MR. TOSO, MR. ERDMANN, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

Lt. Governor Wrigley thanked Mr. Schulz, Ms. Flanagan, Ms. Murtha, Mr. Schaibley, BND, and the SIB for bringing a closure to this issue.

The SIB recessed at 10:25 am and reconvened at 10:40 am.

Westridge/WG Trading – Ms. Murtha informed the SIB the Second Circuit Court of Appeals affirmed the District Court ruling approving the Receiver's plan for a pro-rata distribution and briefly discussed the court's analysis. Ms. Flanagan indicated that the SIB invested $75.3 million with Westridge/WG Trading on behalf of the Pension and Insurance Trusts, and thus far two distributions totaling approximately $67.1 million have been received. Ms. Murtha also stated that it was her understanding the Receiver was still pursuing clawback actions, which if successful, could result in further distributions to the SIB.

GOVERNANCE:

Search Committee – Mr. Sandal updated the SIB on the Executive Director/Chief Investment Officer search.

An RFP for Executive Recruitment Services was issued on March 6, 2013. The deadline for receipt of proposals was March 27, 2013. Six proposals were received with three being rejected by State Procurement. Of the three firms reviewed by the sub-set of the Search Committee and State Procurement, none of them brought forth the required experience.

The sub-set of the Search Committee revised the mandatory requirements to more accurately reflect the criteria needed and instructed State Procurement to reissue the RFP. The RFP was reissued on April 4, with proposals due by April 18, 2013. Six proposals were again received with two being rejected by State Procurement. The sub-set of the Search Committee and State Procurement evaluated the four remaining firms and a decision was made to award the contract. The sub-set of the Search Committee will make their recommendation to the full Search Committee at its next meeting on April 26, 2013.

Compensation Committee – Ms. Ternes, Chair, Treasurer Schmidt, and Mr. Erdmann, serving on the Executive Compensation Review Committee, met on April 23, 2013, and issued the following recommendations for the SIB's consideration:

Issue the Deputy Executive Director a base salary increase of 5% and a temporary Interim Executive Director salary increase of 7.5%, effective July 1, 2013.

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. SANDAL AND CARRIED ON A ROLL CALL VOTE TO GRANT THE DEPUTY EXECUTIVE DIRECTOR A 5% BASE SALARY INCREASE AND A TEMPORARY INTERIM EXECUTIVE DIRECTOR SALARY INCREASE OF 7.5%, EFFECTIVE JULY 1, 2013.

AYES: MR. TOSO, TREASURER SCHMIDT, MR. CORNEIL, COMMISSIONER GAEBE, MR. ERDMANN, MR. SANDAL, COMMISSIONER HAMM, MR. GESSNER, MR. SAGE, MS. TERNES, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

Issue the Deputy Chief Investment Officer a base salary increase of 7%, effective July 1, 2013, and also grant a temporary Interim Chief Investment Officer salary increase of 20%, retroactive to April 1, 2013, and carried forward and applied to the new base salary that is in effect July 1, 2013.

IT WAS MOVED BY MR. ERDMANN AND SECONDED BY TREASURER SCHMIDT AND CARRIED ON A ROLL CALL VOTE TO GRANT THE DEPUTY CHIEF INVESTMENT OFFICER A BASE SALARY INCREASE OF 7%, EFFECTIVE JULY 1, 2013, AND A TEMPORARY INTERIM CHIEF INVESTMENT OFFICER SALARY INCREASE OF 20%, RETROACTIVE TO APRIL 1, 2013, AND CARRIED FORWARD AND APPLIED TO THE NEW BASE SALARY THAT IS IN EFFECT JULY 1, 2013.

AYES: COMMISSIONER HAMM, MS. TERNES, COMMISSIONER GAEBE, MR. GESSNER, MR. SAGE, MR. ERDMANN, MR. SANDAL, MR. TOSO, MR. CORNEIL, TREASURER SCHMIDT, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

2013-14 Meeting Schedule **–** A tentative meeting schedule was established for the 2013-14 fiscal year for the SIB's consideration.

IT WAS MOVED BY MR. SANDAL AND SECONDED BY MR. CORNEIL AND CARRIED ON A ROLL CALL VOTE TO ACCEPT THE TENTATIVE MEETING SCHEDULE.

AYES: MR. GESSNER, COMMISSIONER GAEBE, MR. SAGE, TREASURER SCHMIDT, MR. TOSO, COMMISSIONER HAMM, MR. CORNEIL, MR. ERDMANN, MR. SANDAL, MS. TERNES, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

LEGISLATIVE UPDATE:

Ms. Flanagan provided an update on legislation and reviewed the following bills with the SIB; HB 1022 – RIO Budget Bill, HB 1167 – relating to the definition of earnings of the Legacy Fund, HB 1249 – relating to the membership of the State Investment Board, HB1304 – relating to the divestiture of state investment funds in certain companies liable to sanctions under the Iran Sanctions Act of 1996;

and to provide an expiration date, HB1395 – relating to membership of the Legacy and Budget Stabilization Fund Advisory Board, SB2124 - provides for the legislative management to study methods to assure that the Legacy Fund provides the lasting benefits intended by the voters, and HCR3018 – relating to transfer of a portion of the earnings of the Legacy Fund to the Legacy Scholarship Fund.

Ms. Flanagan stated all bills affecting the SIB have now been finalized by both the House and Senate.

MONITORING REPORTS – The following monitoring reports were presented to the SIB for the quarter ending March 31, 2013; Budget/Financial Conditions, Executive Limitations/Staff Relations, Investment Program Ends, and Retirement Program Ends. A current “Watch List” was also provided for the SIB’s consideration.

IT WAS MOVED BR MR. CORNEIL AND SECONDED BY MS. TERNES AND CARRIED ON A ROLL CALL VOTE TO ACCEPT THE MONITORING REPORTS AS PRESENTED.

AYES: MR. CORNEIL, MR. GESSNER, MR. SANDAL, MR. SAGE, MR. ERDMANN, MR. TERNES, COMMISSIONER HAMM, COMMISSIONER GAEBE, MR. TOSO, TREASURER SCHMIDT, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

OTHER:

The next SIB meeting is scheduled for May 17, 2013, at 8:30 am in the Peace Garden Room at the State Capitol.

The next Audit Committee meeting is scheduled for May 17, 2013, at 1:00 pm in the Peace Garden Room at the State Capitol.

ADJOURNMENT:

With no further business to come before the SIB, Lt. Governor Wrigley adjourned the meeting at 11:10 a.m.

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Lt. Governor Wrigley, Chair
State Investment Board

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Bonnie Heit
Assistant to the Board

STATE INVESTMENT BOARD SEARCH COMMITTEE
MINUTES OF THE
APRIL 26, 2013, MEETING

BOARD MEMBERS PRESENT:	Lt. Governor Wrigley, Chair Levi Erdmann, PERS Board Lance Gaebe, Land Commissioner Mike Gessner, TFFR Board Mike Sandal, PERS Board Kelly Schmidt, State Treasurer Cindy Ternes, WSI Board Bob Toso, TFFR Board
STAFF PRESENT:	Bonnie Heit, Office Manager Fay Kopp, Interim Executive Director Darren Schulz, Interim CIO
OTHERS:	Tricia Opp, State Procurement

CALL TO ORDER:

A meeting of the State Investment Board Search Committee was called to order on Friday, April 26, 2013, at 11:10 am at Workforce Safety & Insurance, 1600 E Century, Bismarck, ND.

The meeting was held for the purposes of reviewing the evaluation results of the second group of proposals received from the Request for Proposal that was issued on April 4, 2013, for the Executive Recruitment Services for the ND Retirement and Investment Office.

Six proposals were received with four company's meeting State Procurement's criteria for further review and consideration. Proposals were received and reviewed from KornFerry International, EFL Associates, Alliance Resource Consulting, and Tunlaw Partners. After evaluating the four remaining proposals, the subset recommended the Search Committee award the contract to KornFerry International. The sub-set felt KornFerry, particularly, Mr. Michael Kennedy, a Senior Client Partner who will lead the search, stood out amongst the other firms due to the fact that he has served as a trustee of the Georgia Employees Retirement System pension fund (serving five years as Chairman of the Board) and is currently serving as chair of its Investment Committee. Mr. Kennedy has also been actively involved in organizations including the Council of Institutional Investors, the National Association of Securities Professionals, and the National Association of State Retirement Administrators, and has attended numerous investment conferences. Mr. Kennedy also serves as chairman of the Federal Retirement Thrift Investment Board accepting President Obama's appointment on August 22, 2011.

After discussion of the proposal results and the sub-set's recommendation, the Search Committee concurred with the sub-set's recommendation to award the Executive Recruitment Services contract to KornFerry.

IT WAS MOVED BY TREASURER SCHMIDT AND SECONDED BY MR. TOSO AND CARRIED ON A VOICE VOTE TO AWARD THE EXECUTIVE RECRUITMENT SERVICES CONTRACT OF THE ND RETIREMENT AND INVESTMENT OFFICE TO KORNFERRY INTERNATIONAL AND INSTRUCTED STATE PROCUREMENT TO FINALIZE THE PROCESS ON BEHALF OF THE SIB.

AYES: COMMISSIONER GAEBE, TREASURER SCHMIDT, MR. SANDAL MR. TOSO, AND LT. GOVERNOR WRIGLEY
NAYS: NONE
MOTION CARRIED

Ms. Opp will issue a notice of an intent to award which is followed by a seven day protest period. On May 6, 2013, the protest period will be completed and if there are no rebuttals, Ms. Opp will start proceedings to issue the contract to KornFerry. The Search Committee thanked Ms. Opp for her assistance.

OTHER:

Mr. Toso informed the Search Committee of his retirement effective June 30, 2013, and informed the Search Committee the Teachers' Fund for Retirement Board recommended Mr. Gessner serve on the Search Committee in his place effectively immediately. The Search Committee accepted the recommendation.

ADJOURNMENT:

With no further issues to come before the Search Committee, the meeting adjourned at 11:20 a.m.

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Lt. Governor Wrigley, Chair
State Investment Board Search Committee

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Bonnie Heit
Assistant to the Board

STATE INVESTMENT BOARD SEARCH COMMITTEE
MINUTES OF THE
APRIL 25, 2013, MEETING

BOARD MEMBERS PRESENT: Lance Gaebe, Land Commissioner
Mike Sandal, PERS Board
Kelly Schmidt, State Treasurer

STAFF PRESENT: Bonnie Heit, Office Manager

OTHERS: Tricia Opp, State Procurement
Darren Schulz, Interim Chief Investment Officer

CALL TO ORDER:

A meeting of a sub-set of the State Investment Board Search Committee was called to order on Thursday, April 25, 2013, at 1:00 pm at the State Treasurer's Office, State Capitol 3rd Fl, Bismarck, ND.

The meeting was held for the purposes of reviewing the Committee's evaluation results of the second group of proposals received from the Request for Proposal that was issued on April 4, 2013, for the Executive Recruitment Services for the ND Retirement and Investment Office.

Six proposals were received. One company was eliminated for late submission of their proposal and the other company was eliminated for not meeting the required experience. Ms. Opp stated the Committee's evaluation results rated the following firm's highest to lowest respectively; KornFerry International, EFL Associates, Alliance Resource Consulting, and Tunlaw Partners.

After discussion of the evaluation results, the Committee was in agreement to award the contract to KornFerry. The Committee will make their recommendation to the full Search Committee at their April 26, 2013, meeting which will take place after the State Investment Board's regularly scheduled meeting on April 26, 2013.

ADJOURNMENT:

With no further issues to come before the Committee, the meeting adjourned at 1:35 p.m.

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State Investment Board Search Committee

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Bonnie Heit
Assistant to the Board

STATE INVESTMENT BOARD SEARCH COMMITTEE
MINUTES OF THE
APRIL 3, 2013, MEETING

BOARD MEMBERS PRESENT:	Lance Gaebe, Land Commissioner Mike Sandal, PERS Board Kelly Schmidt, State Treasurer
STAFF PRESENT:	Bonnie Heit, Office Manager
OTHERS:	Tricia Opp, State Procurement

CALL TO ORDER:

A meeting of a sub-set of the State Investment Board Search Committee was called to order on Wednesday, April 3, 2013, at 1:40 pm at the State Treasurer's Office, State Capitol 3rd Fl, Bismarck, ND.

The meeting was held for the purposes of reviewing the Committee's evaluation results of the proposals received for the Executive Recruitment Services for the ND Retirement and Investment Office.

The Committee discussed their evaluation results and determined that of the three firms evaluated, none of them brought forth the required experience, specialization, and history of successfully recruiting an investment professional such as the State Investment Board is seeking.

After further discussion,

MR. SANDAL MOVED AND TREASURER SCHMIDT SECONDED TO REISSUE THE REQUEST FOR PROPOSAL FOR EXECUTIVE RECRUITMENT SERVICES FOR THE ND RETIREMENT AND INVESTMENT OFFICE.

AYES: MR. SANDAL, TREASURER SCHMIDT, COMMISSIONER GAEBE
NAYS: NONE

MOTION CARRIED

The Committee reviewed the mandatory requirements and revised the language to more accurately reflect the criteria needed and instructed Ms. Opp to reissue the Request for Proposal as soon as possible with a due date of April 18, 2013.

ADJOURNMENT:

With no further issues to come before the Committee, the meeting adjourned at 2:30 p.m.

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State Investment Board Search Committee

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Bonnie Heit
Assistant to the Board

STATE INVESTMENT BOARD SEARCH COMMITTEE
MINUTES OF THE
MARCH 28, 2013, MEETING

BOARD MEMBERS PRESENT:	Lance Gaebe, Land Commissioner Mike Sandal, PERS Board Kelly Schmidt, State Treasurer
STAFF PRESENT:	Bonnie Heit, Office Manager
OTHERS:	Tricia Opp, State Procurement

CALL TO ORDER:

A meeting of a sub-set of the State Investment Board Search Committee was called to order on Thursday, March 28, 2013, at 1:30 pm at the State Procurement Office, State Capitol 14th Fl, Bismarck, ND.

The meeting was held for the purposes of reviewing the proposals received for the Executive Recruitment Services for the ND Retirement and Investment Office. The Request for Proposal (RFP) was issued March 6, 2013, with proposals due by March 27, 2013, at 3:00 p.m., CT. State Procurement received six proposals of which three were rejected for failure to submit their proposal by the required due date.

Ms. Opp reviewed the RFP evaluators guide with the Committee. Each Committee member will evaluate the proposals and submit their scores to Ms. Opp. The Committee will meet again on April 3, 2013, to discuss the results. The Committee also tentatively scheduled April 5, 2013, for phone interviews. The contract is tentatively scheduled to be awarded on April 8, 2013. Once the award is made, all of the proposals received become open record. The firm awarded the contract will start approximately May 1, 2013.

ADJOURNMENT:

With no further issues to come before the Committee, the meeting adjourned at 2:10 p.m.

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State Investment Board Search Committee

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Bonnie Heit
Assistant to the Board

MEMORANDUM

TO: TFFR Board

FROM: Fay Kopp

DATE: May 9, 2013

SUBJ: 2013-14 TFFR Board Calendar and Education Plan

Enclosed is an updated 2013-14 TFFR Board calendar and education plan. Your suggestions for educational or other board meeting topics are welcome.

I have also included information from various entities relating to upcoming board educational conferences and workshops.

NCTR

Trustee Workshop	July 29-31, 2013	Boston, MA
Annual Convention	Oct. 5- 9, 2013	Washington DC

Callan College

Intro to Investments	Oct. 29-30, 2013	San Francisco, CA
Standard Session	July 16-17, 2013	Chicago, IL

International Foundation of Employee Benefit Plans

Certificate in Retirement Plans	July 16-21, 2013	Brookfield, WI
	Sep 30-Oct 5, 13	Seattle, WA
Advanced Investments Mgmt	Sept 9-12, 2013	Philadelphia, PA
CAPPP, Part 1 – Pensions	Oct. 19-20, 2013	Las Vegas, NV
Trustees Masters Program	Oct. 19-20, 2013	Las Vegas, NV
Employee Benefits Conf	Oct. 20-23, 2013	Las Vegas, NV
Benefits Conf – Public Employees	April 2014?	
Investments Institute	April 2014?	
Portfolio Concepts and Mgmt	May 2014?	
CAPPP, Part 1 – Pensions	June 2014?	
CAPPP, Part 2 – Pensions	June 2014?	

TFFR Board Calendar and Education Plan 2013-14

JULY 25, 2013 – 1 pm
Election of officers
TFFR Board Accomplishments
Annual TFFR Program Review
Annual Customer Satisfaction Reports
Legislative update
Education: Retirement plan overview

SEPTEMBER 26, 2013 – 1 pm
Annual TFFR investment review
Annual RIO budget and expense report
Legislative update
Education: Fiduciary duties/ethics

OCTOBER 24, 2013 – 1 pm
2013 actuarial valuation report – Segal
GASB - Segal
Annual TFFR program audit report
Annual TFFR Ends and Statistics
Legislative update

JANUARY 23, 2014 – 1 pm
2015 Legislative planning
Annual pension plan comparisons
– 2013 Public Pension Survey
Annual Retirement Trends Report
Education: Open records/meetings

MARCH 27, 2014 – 1 pm
2015 legislative planning
Approve bills for interim LEBPC study
Education: Employer reporting overview

APRIL 24, 2014 – 1 pm
Legislative update
Annual Technology Review
2014-15 board calendar and work plan
Education:

05/09/13

NATIONAL COUNCIL ON TEACHER RETIREMENT

Supporting Retirement Security for America's Teachers

Join Login

Trustee Education

13th Annual Trustee Workshop: July 29-31, 2013

in conjunction with the John F. Kennedy School of Government at Harvard University - Registration Opens in May 2013

The 13th Annual Trustee Workshop will be hosted in conjunction with the John F. Kennedy School of Government at Harvard University in late July.

Registration opens in May! More information on the Trustee Workshop coming soon!

Registration Fee for Trustee Workshop: $1200/attendee

Guest Fee: $150/guest

ARCHIVE: 2012 Trustee Institute and Workshop

9370 Studio Court, Suite 100E, Elk Grove, CA 95758
PH 916-897-9139 | FAX 916-897-9315

NCTR

NATIONAL COUNCIL ON TEACHER RETIREMENT

Supporting Retirement Security for America's Teachers

Join Login

Home | About | Convention | Federal Governmental Relations | Education | Member Directory | News | Resources

91st Annual Convention

Pensions and Politics; The New Realities!

October 5-9, 2013

91st Annual Convention

"Pensions & Politics; The New Realities!"

October 5-9, 2013

Registration opens in June!!

Sponsorship Opportunities

Interested in sponsoring NCTR's 91st Annual Convention? Email us at contactnctr@nctr.org for details!

ARCHIVE: 90th Annual Convention

Attendee List

Presentations and Committee Reports

Online Registration

Registration for our 91st Annual Convention in Washington, D.C. will open in June 2013.

Registration Fees:

Member (Non-Commercial):
$900/attendee
$250/guest

Member (Commercial Associate):
$1850/attendee
$350/guest

Lodging Information

Reserve after Registration

Your reservation link will be provided to you in your registration confirmation email.

Omni Shoreham Hotel
2500 Calvert Street NW
(at Connecticut Ave.)
Washington, D.C. 20008

9370 Studio Court, Suite 100E, Elk Grove, CA 95758
PH 916-897-9139| FAX 916-897-9315

This course is beneficial to anyone involved in the investment management process.

Contact Us

For more information on the "Callan College," contact Kathleen Cunnie at college@callan.com.

Standard Session

July 16-17, 2013 – Chicago, IL

Sample Agenda
Hotel Information
Register

The Standard Session of the "Callan College" will be taking place at Callan's Chi Office located on the 35th floor of 120 North La Salle Street.

This is a two day session designed for individuals with more than two years' experience with institutional asset management oversight and/or support responsibilities. The session will provide attendees with a thorough overview of prudent investment practices for both defined benefit and defined contribution fu We cover the key concepts needed to successfully meet a fund's investment objectives.

The course work addresses the primary components of the investment manager process:

The Role of the Fiduciary
Capital Market Theory
Asset Allocation
Manager Structure
Investment Policy Statements
Manager Search
Custody, Securities Lending, Fees
Performance Measurement

This course is beneficial to anyone involved in the investment management proc including: trustees and staff members of public, corporate and Taft-Hartley retire funds (defined benefit and/or defined contribution); trustees and staff members c endowment and foundation funds; representatives of family trusts; and investme management professionals and staff involved in client service, business develop consultant relations, and portfolio management.

Tuition for the Standfard "Callan College" session is $2,500 per person. Tuition includes instruction, all materials, breakfast and lunch on each day, and dinner o first evening with the instructors.

This two day session is designed for individuals who have less than two years' experience with institutional asset management oversight and/or support responsibilities.

Contact Us

For more information on the "Callan College," contact Kathleen Cunnie at college@callan.com.

Introduction to Investments

October 29-30, 2013 - San Francisco

Sample Agenda
Register

This one and one half day session is designed for individuals who have less thai years' experience with institutional asset management oversight and/or support responsibilities. The session will familiarize fund sponsor trustees, staff, and ass management advisors with basic investment theory, terminology, and practices.

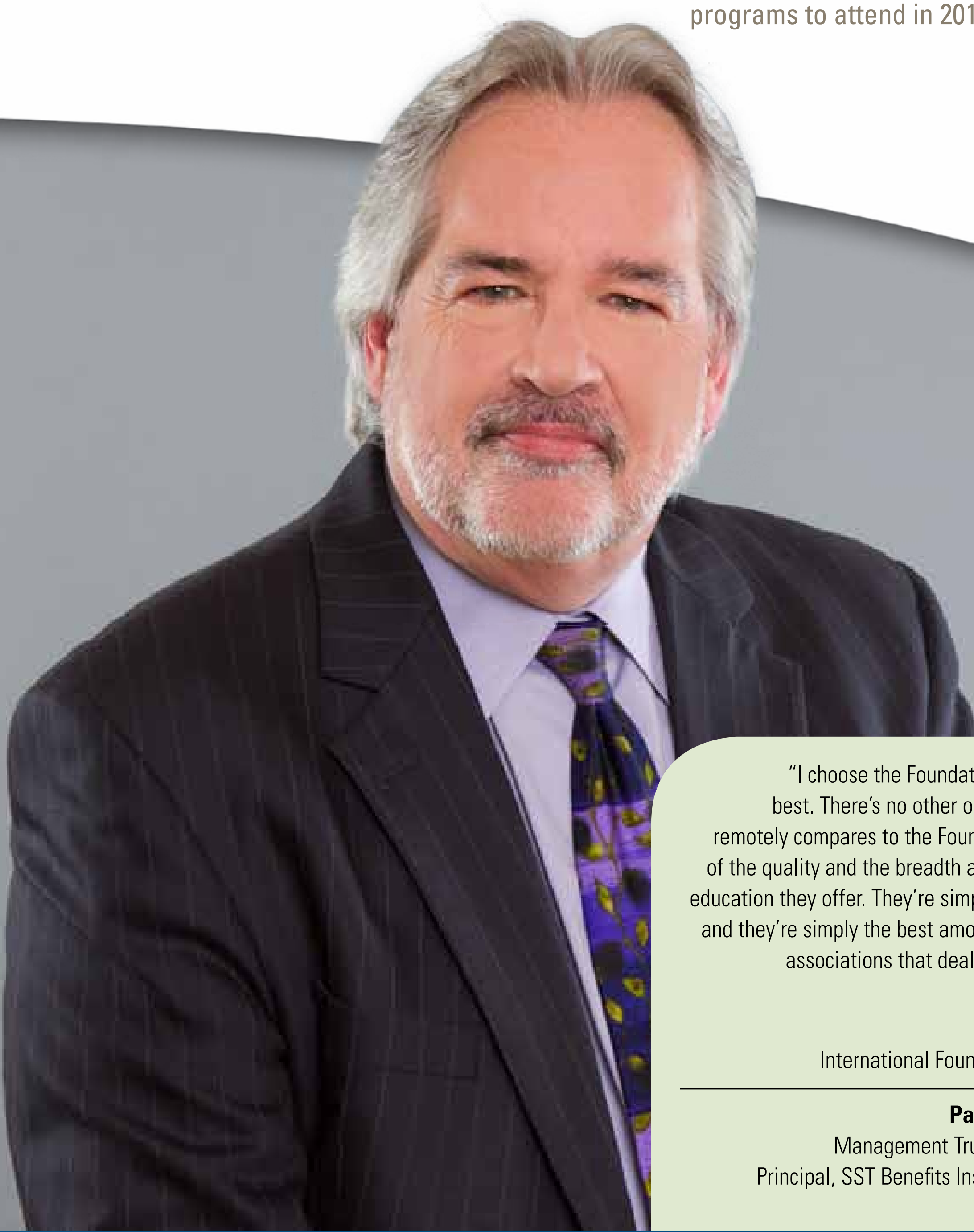
Participants in the introductory session will gain a basic understanding of the diff types of institutional funds, including a description of their objectives and investn program structures. The session includes:

- A description of the different parties involved in the investment management process, including their roles and responsibilities
- A brief outline of the types and characteristics of different Plans (e.g.,defined I defined contribution, endowments, foundations, operating funds)
- An introduction to fiduciary issues as they pertain to Fund management and oversight
- An overview of capital market theory, characteristics of various asset classes, the processes by which fiduciaries implement their investment sessions

Tuition for the Introductory "Callan College" session is $2,350 per person. Tuitioi includes instruction, all materials, breakfast and lunch on each day, and dinner o first evening with the instructors.

Suggested Training Path for Public Sector Trustees and Staff

Save this guide for reference as you select the programs to attend in 2013 and beyond.



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International Foundation Member

Paul Hackleman
Management Trustee SamCERA
Principal, SST Benefits Insurance Service

www.**ifebp.org**/educationpath

International Foundation
OF EMPLOYEE BENEFIT PLANS

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	PENSION TRUSTEE	HEALTH TRUSTEE
Basic (1-2 Years)	**Conference** Benefits Conference for Public Employees	**Conference** Benefits Conference for Public Employees
	Designation and Certificate Courses CAPPP™ Part I—Pensions Portfolio Concepts and Management (Wharton)	**Designation and Certificate Courses** CAPPP™ Part I—Health Portfolio Concepts and Management (Wharton)
	E-Learning Courses Overview of Retirement Plans Investment Basics	**E-Learning Courses** Introduction to Health Care and Group Benefit Plans Health Care Reform
	Books *Benefits and Compensation Glossary* *Wellness Programs and Value-Based Health Care*	**Books** *Benefits and Compensation Glossary* *Wellness Programs and Value-Based Health Care*
Intermediate (3-4 Years)	**Conferences** Benefits Conference for Public Employees Investments Institute	**Conferences** Benefits Conference for Public Employees Health Care Management Conference
	Designation and Certificate Courses CAPPP™ Part II—Pensions Certificate in Retirement Plans (Certificate Series) Advanced Investments Management (Wharton)	**Designation and Certificate Courses** CAPPP™ Part II—Health Certificate in Health Care Plans (Certificate Series)
	E-Learning Courses Defined Benefit Plans Defined Contribution Plans	**E-Learning Courses** Wellness and Disease Management Short- and Long-Term Disability
Advanced (5+ Years)	**Conferences** Benefits Conference for Public Employees Investments Institute	**Conferences** Benefits Conference for Public Employees Health Care Management Conference
	Designation and Certificate Courses Hedge Funds, Real Estate and Other Alternative Investments (Wharton) International Investing and Emerging Markets (Wharton) Retirement Plans Associate (RPA) Designation Certified Employee Benefit Specialist (CEBS) Designation	**Designation Course** Certified Employee Benefit Specialist (CEBS) Designation

ADMINISTRATIVE STAFF

Conference
Benefits Conference for Public Employees

Designation and Certificate Courses
Certificate in Public Sector Benefits Administration (Certificate Series)
Certificate in Retirement Plans (Certificate Series)
Certificate in Health Care Plans (Certificate Series)

E-Learning Courses
Overview of Retirement Plans
Introduction to Health Care and Group Benefit Plans
Introduction to Compensation

Books
Benefits and Compensation Glossary
Wellness Programs and Value-Based Health Care

Conferences
Benefits Conference for Public Employees
Benefit Communication and Technology Institute (2014)

Designation and Certificate Courses
Group Benefits Associate (GBA) Designation
Compensation Management Specialist (CMS) Designation

E-Learning Courses
Investment Basics
Family and Medical Leave Act (FMLA)
HIPAA Security
HIPAA Privacy

Conferences
Benefits Conference for Public Employees
Health Care Management Conference
Investments Institute

Designation and Certificate Courses
Group Benefits Associate (GBA) Designation
Compensation Management Specialist (CMS) Designation
Certified Employee Benefit Specialist (CEBS) Designation

Plus ONE or MORE of the following comprehensive or specialty offerings each year.

COMPREHENSIVE AND SPECIALTY EDUCATIONAL OPTIONS

Comprehensive Conference
Annual Employee Benefits Conference

Specialty Conferences
Washington Legislative Update
Benefit Communication and Technology Institute* (2014)

Specialty Designations and Certificate Courses
Certificate in Benefits and Compensation Management (Certificate Series)
Retirement Plans Associate (RPA) Designation
Compensation Management Specialist (CMS) Designation
Group Benefits Associate (GBA) Designation
Certified Employee Benefit Specialist (CEBS) Designation

Specialty E-Learning Courses
Fiduciary Responsibility
HSAs/HRAs
The Americans with Disabilities Act (ADA)
Life and Accidental Death and Dismemberment
Health Care Reform
COBRA
Short- and Long-Term Disability
Introduction to Compensation
Family and Medical Leave Act (FMLA)
HIPAA Privacy
HIPAA Security
Health Care Exchanges Regulations and Their Impact on Employers and Individuals

Specialty Books
Healthy Employees, Healthy Business: Easy, Affordable Ways to Promote Workplace Wellness
Pharmacy Benefits: Plan Design and Management
Health Insurance Answer Book

Foundation Web Pages
Health Care Reform Central
Value-Based Health Care
Retirement Security

Webcasts
New Webcasts are typically offered twice a month for timely updates on emerging trends and issues in a range of topic areas that include health care, retirement, legal and legislative, wellness and general human resources. Visit www.ifebp.org/webcasts for list of upcoming live Webcasts.

*Programs offered every other year

2013 Public Sector Program Schedule

Date	Program	Location
February 18-23	Certificate Series www.ifebp.org/certificateseries	Lake Buena Vista (Orlando), Florida
March 11-13	Health Care Management Conference www.ifebp.org/healthcare	Rancho Mirage, California
April 16-17	Benefits Conference for Public Employees www.ifebp.org/peconference	Sacramento, California
April 22-24	Investments Institute www.ifebp.org/investments	Phoenix, Arizona
May 6-9 (tentative)	Portfolio Concepts and Management www.ifebp.org/wharton	Philadelphia, Pennsylvania
May 20-21	Washington Legislative Update www.ifebp.org/washington	Washington, D.C.
June 25-26	Certificate of Achievement in Public Plan Policy (CAPPP™)—Pensions and Health Part I www.ifebp.org/cappp	Chicago, Illinois
June 27-28	Certificate of Achievement in Public Plan Policy (CAPPP™)—Pensions and Health Part II www.ifebp.org/cappp	Chicago, Illinois
July 16-21	Certificate Series www.ifebp.org/certificateseries	Brookfield, Wisconsin
September 9-12 (tentative)	Advanced Investments Management www.ifebp.org/wharton	Philadelphia, Pennsylvania
September 22-25	32nd Annual ISCEBS Employee Benefits Symposium www.ifebp.org/symposium	Boston, Massachusetts
September 30-October 5	Certificate Series www.ifebp.org/certificateseries	Seattle, Washington
October 19-20	Administrators Masters Program® (AMP®) www.ifebp.org/amp	Las Vegas, Nevada
October 19-20	Certificate of Achievement in Public Plan Policy (CAPPP™)—Pensions and Health Part I www.ifebp.org/cappp	Las Vegas, Nevada
October 19-20	Trustees Masters Program® (TMP®) www.ifebp.org/tmp	Las Vegas, Nevada
October 19-20	TMP® Advanced Leadership Summit www.ifebp.org/tmpsummit	Las Vegas, Nevada
October 20-23	59th Annual Employee Benefits Conference www.ifebp.org/usannual	Las Vegas, Nevada

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Public pension funds face scrutiny from accounting updates

By: Hazel Bradford , Published: April 1, 2013 Pensions & Investments

Public pension executives are facing a paperwork tsunami this year.

Not only do new financial reporting rules from the Governmental Accounting Standards Board start going into effect this June, but Moody's Investors Service Inc. is implementing — starting this month — a new set of calculations that puts pension debt front and center in rating state and local governments.

“Moody's introducing a third set of calculations is only going to exacerbate the confusion and the selective use by people finding the pension number that fits their agenda,” said Keith Brainard, director of research in Georgetown, Texas, for the National Association of State Retirement Administrators.

When issuing the proposed change, Moody's officials noted that by their calculations, some $3 trillion in state and local unfunded pension liabilities were roughly triple what governments were reporting. To get a better sense of long-term liabilities and how they affect overall debt, and to allow for more comparability of plans' long-term liabilities, the New York-based ratings agency said it will now ask for more information, including:

accrued actuarial liabilities based on a high-grade long-term corporate bond index discount rate, currently around 5.5%; the market value of assets, instead of more common asset smoothing; pension contributions spread over a common amortization period of 17 years; and multiple-employer cost-sharing plans' portion of pension liabilities based on contributions to larger, state-run plans.

Consider recent changes

Officials at Moody's, which has collected data for 8,500 local governments and 14,000 public pension plans, say they will also consider recent plan changes or reforms not yet reflected in pension reports.

“Comparable disclosure across plans is a very worthwhile goal that helps inform bondholders and others,” said Donald Fuerst, senior pension fellow at the American Academy of Actuaries, Washington, which supports more consistent disclosure of public plan assets and liabilities. But he worries that without complete demographic data for each plan, “the methodology is going to be somewhat simplistic” and thus may have limited value or impact. “I don't think it's going to have any real significant change in how things go,” he said in an interview.

It will have “a dramatic change on government balance sheets,” said John Tuohy, Arlington County (Va.) deputy treasurer, who chairs the pension committee of the Government Finance Officers Association, Washington. “But what are they trying to accomplish? We fund so much of what we do through debt, which is short term, while pension obligations stretch out years. It really is a huge distinction.”

GFOA members are particularly concerned about pension funds “at or slightly above doing the right thing,” Mr. Tuohy said in an interview. “The reality is that nothing has changed for them, but you're tossing them into the concern bucket. I worry about them because the practical effect is the cost of the debt. That turns into real money, and that money has to come from somewhere.” Even for a solid pension system like the $1.7 billion Arlington County Employees' Retirement System, which is funded around 91%, Moody's review could cause that to drop as low as 75% by some unofficial calculations “while the circumstances haven't changed at all,” he said.

Along with the immediate spike in pension liabilities expected from the new liability measurements, public pension officials and advocates are also worried about being subjected to a "one-size-fits-all" approach. "Using a single discount rate to measure public pension plans will introduce greater distortion and result in less clarity, not more," officials from the $40.2 billion Maryland State Retirement & Pension System, Baltimore, wrote to Moody's in its September comment letter. "It is difficult to see how the goal of greater comparability among plans will be achieved. ... It is unclear how comparability, even if it were possible, says anything about the state's ability to fulfill its obligations."

A common metric for pension liability "is a very positive step for transparency," maintained Josh McGee, vice president of public accountability at the Laura and John Arnold Foundation in Houston who studies public pension issues, in an interview. "Just like any other debt, (governments) should be worried about how it affects their credit rating. It doesn't actually affect what they owe. Hopefully it will push the others to do a better job of managing debt, and to have governments pay what they promise."

It should also discourage government officials from diverting pension contributions for other purposes, he said. "Taking from the pension fund is convenient, but it is borrowing just like any other debt," which plans should address sooner rather than later. He cited the example of the $116.3 billion Teacher Retirement System of Texas, Austin, which at 80% is relatively well funded, "but has no plan to pay off" that unfunded liability. TRS spokesman Howard Goldman said officials are now working with state legislators to consider options for addressing a $27.4 billion unfunded liability.

Settle in

Public pension and budget officials would prefer that Moody's let GASB rules settle in before adding another measurement and a third number that could confuse public debate. "GASB has done a really good job of highlighting the impact of underfunding. It's going to end up on Moody's to explain why they didn't accept that. They are kind of throwing a rock in the pond," said Mr. Tuohy of Arlington County.

"It's important that people understand that while there are a lot of new calculations going on, the underlying reality of the conditions of these plans and the funding of these plans has not changed. It's incumbent on the public pension community to educate stakeholders on what these different sets of numbers mean," said Mr. Brainard of NASRA.

Mr. McGee of the Arnold Foundation recognizes fears expressed by public plan sponsors and public employee advocates that having a more prominent pension liability number might put more pressure on governments to cut pensions, "but ignoring it simply makes the problem bigger in the future" and risks putting more of the burden on new workers. "The size of the pension debt has become so large that they can't ignore it anymore," Mr. McGee said in an interview.

David Jacobson, spokesman for Moody's public finance group in New York, cautions that state ratings will not experience any immediate change, and less than 2% of plans are likely to go under review for possible downgrade. Further, he said, with pensions just one of many factors, any resulting downgrades "are likely to be limited to two notches."

But David Madland, director of the American Worker Project at the Center for American Progress in Washington, worries that Moody's "misguided" mission "could make (public pension systems) appear far more underfunded than they are and more expensive, and probably hasten their decline."

GOVERNING
THE STATES AND LOCALITIES

Moody’s Investors Service on Wednesday announced its highly anticipated new ratings rules, in a move that could result in downgrades for dozens of school districts and municipal governments, including Chicago, Cincinnati, Santa Fe, Minneapolis, and Portland, Ore.

Under the new rules, Moody's is revamping the way it analyzes and adjusts pension liabilities as part of its credit analysis of state and local governments. These changes reflect a view that pension obligations are “a significant source of credit pressure for governments and warrant a more conservative view of the potential size of the obligations,” according to a press release announcing the new rules. As a result of the new approach, Moody's immediately placed on review the general obligation bonds for 29 municipalities that have large adjusted net pension liabilities. Those bonds now face a possible downgrade.

"Pension obligations represent a growing source of budgetary pressure for many governments. However, the manner in which these obligations are reported varies widely, and we believe liabilities are underreported from a balance sheet perspective," Timothy Blake, a Moody's managing director, said in a statement. "The purpose of the adjustments is to provide greater transparency and comparability in pension liability measures for use in credit analysis."

The new rules differ slightly from the agency’s original proposal from last summer. But the plan to adjust pension debt using a long term bond index rate remains intact. (Moody's did adjust that proposal to use the bond index rate posted as of the valuation date of each plan.) Moody's new discount rate will likely result in rates of return that are smaller than the 7 to 8 percent assumption over 30 years that most governments use in calculating their pension liabilities. In its explanation, Moody's said its approach estimates the value of expected benefit payments by current employees over their careers using current market interest rates as the guide to the current value of future cash flows.

“Because interest rates are currently at an historic low, the market approach to measuring liabilities results in much larger current total liabilities than those reported using the conventional governmental approach,” the agency report detailing the changes said.

In other new rules, asset smoothing will be replaced with reported market or fair value as of the actuarial reporting date and the resulting adjusted net pension liability will be amortized over 20 years. A shorter amortization period would also have the effect of increasing pension liabilities as most state and local governments use the 30-year amortization period (a Generally Accepted Accounting Principle). The original proposed change had a 17-year amortization period, a number based on the estimated service time left for the average municipal worker.

The report noted that just 2 percent of governments were likely to have their rating affected by the new rules.

“As pensions are just one of many factors we consider in a rating, any downgrades resulting from the subsequent reviews are likely to be limited to two notches,” the report said. “The affected ratings will be for those local governments whose adjusted pension obligations relative to their resources place them as significant outliers in their current rating categories.”

4 Myths About Public Pension Retirees

BY: Liz Farmer | March 8, 2013

Think public retirees have it made? Not necessarily.

True, there have been plenty of headline-grabbing cases of public-sector retirees with seemingly over-generous pensions -- even some whose retirement pay outstrips what they made in their working days. But the fact is that most public retirees enjoy modest lifestyles.

Still, in the ongoing debate over reforming public pensions, retirees sometimes are portrayed as living high on the hog, a characterization employee advocates say is unfair -- and one that's clouding the issue.

Here, then, are a few of what retiree advocates say are the biggest myths about public pensions.

1. Retirement benefits make people rich.

Pension spiking has been a problem, to be sure. But most retirees' pay is decidedly modest.The average federal pensioner receives about $32,000 per year, while state and local average payouts vary. Washington state’s average pension benefit, for example, is about $21,500 annually, according to the Washington Policy Center. New York state’s payouts to police and fire retirees average $42,259 annually. State and local employees in New York receive an average of $20,200 annually, according to the Office of the Comptroller.

None of those figures could be called extravagant, says Keith Brainard, research director for the National Association of State Retirement Administrators. Retirement security – not wealth building – is the name of the game for the typical public retiree. “There’s nothing wrong with wealth creation,” Brainard says, “but the first purpose of retirement benefits ought to be to make sure people have a roof over their head and food on the table.”

2. What a racket! Some retirees didn’t even have to contribute to their plans for their entire career!

Yep, it's true that some employees, particularly those hired in the boom years of the 1990s, didn't pay in to the system. And now some of those people are reaping pensions in retirement.

But it's more accurate to say that the setup was the result of a broken system rather than the result of freeloading employees. Many governments took a so-called “funding holiday” in the 1990s as pension funds swelled thanks to a rising market. (Of course, those states failed to acknowledge that bad years often follow good ones. As the economy stalled over the past decade, those contribution holidays aggravated the impact of market losses.)

The idea that employees somehow gamed the system is unfair, says Melissa Turner, an employee at the University of California at Davis who was hired during that time period. After all, individual employees don’t have control over how their retirement savings programs are run.

“I do understand that something needs to change, but you can’t put a freeze on everything for 10 years and then start expecting people to go, ‘Hey, yeah, I’ll pay for a service I already thought I was getting,’” she says, adding, “If they’d just left it the way it was, it would have been different.”

3. The biggest problem is that retirees are living longer.

True, they are. According to the U.S. Census Bureau, the nation's 90-and-older population nearly tripled over the past three decades, reaching 1.9 million in 2010. But increased life expectancy is only a piece of the demographics pie -- another piece is that people are having fewer children today. According to the Social Security Administration (another entity grappling with an aging population), the elderly population will reach 23 percent of the total U.S. population by 2080. That means that the 65-and-over population will have more than doubled as a percentage of the total population in roughly 100 years' time. Meanwhile, the working population is shrinking; it's on track to drop from 60 percent in 2005 to 54 percent in 2080. In short, fewer people will be paying in to pension systems while more people will be receiving their benefits.

Still, the bigger issue, as far as funding pensions goes, has to do with system mismanagement. In addition to the payment holidays during the booming '90s, states and localities were also keen on increasing pension benefits during that time. In California, for example, Gov. Gray Davis in 1999 signed into law a bill that granted billions of dollars in retroactive pension increases to state employees and allowed retirements as young as age 50 with lifetime pensions of up to 90 percent of their final year salaries. It took the state more than a decade to pass reform that essentially undid the 1999 law.

4. It's the economy! These issues were inevitable!

It's not that simple. One of the best-funded pension plans is actually in Illinois, a state that has become a poster child for underfunded pensions. The exception to Illinois’ inability to address its unfunded liability is the 90 percent-funded Illinois Municipal Retirement Fund (IMRF).

“We’re trying to distinguish ourselves from the headlines that typically occur in Illinois,” says Louis Kosiba, the fund’s executive director.

The key difference between IMRF and Illinois’ other major pension plans goes back to management: IMRF has the ability to enforce employers’ payments into the plan. The state of Illinois has been notorious for not putting its required annual payments into its pension plan in recent years, a big factor in its unfunded liability, which hovers just above 40 percent.

“It’s very easy for us to track if someone has fallen off bandwagon,” Kosiba says. “There is a culture here that you pay your required contribution.”

Bill would raise retirement age for public employees

MARCH 16, 2013 1:00 PM • STEVEN VERBURG | WISCONSIN STATE JOURNAL

The minimum retirement age for public employees would increase by two years under a bill proposed by a state lawmaker who said the change would reflect increasing life spans and later retirement ages in general while possibly strengthening the pension system.

Democrats and a prominent retiree group were skeptical, and the state Department of Employee Trust Funds said a thorough actuarial study was needed to make sure the change wouldn't cause unintended problems.

Most municipal workers, state employees and teachers in the Wisconsin Retirement System must work until they are 65 years old to collect full benefits, but they can retire at age 55 with reduced pensions.

Under a bill circulated by Rep. Duey Stroebel, R-Saukville, the minimum age would rise to 57. For police and firefighters, it would increase two years to 52.

"(Current laws) have been in place for many years and have not changed to reflect increased longevity, normal life work span or the changing demographics of our state," Stroebel said Friday in an email sent to state legislators in an effort to find co-sponsors.

Stroebel's bill would affect only people who are under 40, so nobody would be affected for more than a decade.

The average retirement age is 60.

The pension system has been lauded by the Pew Center on the States and others who ranked the system as the best in the nation because it is fully funded.

"He wants to address a problem that doesn't exist," said Jim Palmer, president of a group representing pension system members.

But Stroebel pointed to a 2012 memorandum in which ETF staff told him that while early retirees receive reduced pensions, state law doesn't reduce them enough to completely cover costs.

"The system does take a hit every time there is an early retirement," Stroebel, who is co-chairman of the Legislature's Joint Survey Committee on Retirement Systems, said in an interview. "We value our trust fund greatly and we value its solvency."

The ETF memo also emphasized an actuarial study was needed to know how the change would affect the complex retirement system. For example, adjusting the retirement age could increase costs for taxpayers because experienced workers would stay on the payroll longer. Or it could mean injured or ill employees would continue working, leading to higher costs in disability claims, especially among police and firefighters. "(It also) could degrade the overall policy aim of maintaining public safety at a high level," the department memo said.

Terese Berceau, a Madison Democrat on the retirement committee, said she was wary of reducing flexibility for workers deciding when to retire.

"People do age differently," Berceau said. "There are some people who don't age well, and they may have great difficulty working longer."

The system serves 570,000 employees and retirees. Benefits average about $23,000 a year. They are calculated based on years worked, salary and fund investment income.

About 75 percent of costs are paid by investment proceeds, with the rest coming from contributions made by government employers and employees

Pa. gov plan would freeze current pension benefits

By PETER JACKSON | Posted: Saturday, March 16, 2013 3:46 pm

Gov. Tom Corbett and his legal staff are hoping fine distinctions in Pennsylvania case law will allow $12 billion in cuts to future pension benefits for more than 370,000 current state and school employees.

Corbett and state legislators are grappling with Pennsylvania's unfunded pension liability of $41 billion, and the governor is taking an approach never before tested in state courts in hopes it will help the benefit reductions pass constitutional muster.

"We've designed our proposal in a way we believe it is constitutional, knowing that the likelihood is that that issue will ultimately be litigated in the courts," state Budget Secretary Charles Zogby said.

More than a month after Corbett announced his plan, drawing threats of lawsuits from labor unions, the legislative response has been cool and no bill has been introduced.

The benefit cuts are the main source of savings in Corbett's multi-pronged pension reform package and are expected to save an estimated $12 billion over 30 years. The package also would require new hires to enroll in a 401(k)-style plan, instead of the traditional plan and temporarily limit annual increases in taxpayer contributions.

The governor proposes freezing benefits for current employees and replacing them with reduced benefits in 2015. When workers retire, they would receive the combined value of both sets of benefits.

The change for members of the Public School Employees' Retirement System would occur Jan. 1, 2015; and for workers in the State Employees' Retirement System, on July 1, 2015, officials said. For current employees, the biggest single change in the governor's plan is a reduction in the "multiplier," a percentage applied to an employee's years of service and final average salary to calculate pensions, typically from 2.5 percent to 2 percent.

Over the years, Pennsylvania courts have issued numerous rulings that have established that public pension benefits are contracts and that the state constitution protects them against changes that "impair" that contract.

In a 1984 decision central to the current debate, the state Supreme Court overturned a legislatively approved increase in employee contributions. The justices said the increase represented an unconstitutional impairment of contract because it reduced a pension's value by forcing the employee to pay more for it.

Corbett's legal team says past court rulings on contract impairment have weighed both the retroactive effect of benefit changes and the future impact. By freezing current benefits and locking in their value to employees, the lawyers hope to focus any challenge exclusively on future benefits _ something they say neither the Legislature nor state courts has ever done.

"It's a brand new analysis for the court," said James Schultz, the governor's general counsel. "In short ... the (state) Supreme Court would not be put into a position where it had to overrule itself on prior precedent."

Union leaders who have led the fight against the pension cuts said the novelty of the administration's approach doesn't fundamentally change the facts. "Their legal theory doesn't make any sense to me," said Lynne Wilson, general counsel for the Pennsylvania State Education Association, the state's largest teachers' union.

Sen. Jake Corman, R-Centre, chairman of the Senate Appropriations Committee, said the governor's plan would provide short-term savings to taxpayers but it would not make a significant dent in the already accrued unfunded liability. But he is similarly uncomfortable with such alternatives as pension bonds, which he called "a risky proposition."

"It's a huge issue that has to be dealt with," Corman said. "People are finally coming to the realization that there's no easy answer."

Study says Missouri's public pensions are worse than they appear

MARCH 17, 2013 12:11 AM • BY DAVID NICKLAUS DNICKLAUS@POST-DISPATCH.COM 314-340-8213

Even as neighboring Illinois gets lambasted regularly for having the worst-funded public pension plans in the nation, Missourians have believed their state's plans to be relatively sound.

Now the Show-Me Institute wants to shake us out of that comfort zone. The St. Louis think tank published a study by Andrew Biggs, a scholar at the American Enterprise Institute in Washington, who claims that Missouri's unfunded pension liability is $54 billion, nearly five times the official estimate of $11.1 billion. (*Note: The original version of this column incorrectly stated the amounts in millions instead of billions.)*

By Biggs' calculation, the state's five biggest pension funds have enough assets to cover just 46 percent of their projected liabilities.

The plans themselves claim they are 80.5 percent funded.

It's important to note that no one is accusing the state, or its pension administrators, of doing anything wrong. The funds follow rules set by the Governmental Accounting Standards Board, and Missouri — unlike Illinois — has faithfully made the contributions it was supposed to make.

Biggs, though, says the accounting rules disguise the amount of risk that taxpayers take when they promise to pay a pension decades from now. The discount rate, which pension actuaries use to value those future promises, is at the center of his argument.

Government pensions assume that their discount rate is equal to what they're going to earn on future investments. The Missouri plans use discount rates ranging between 7.25 percent and 8.25 percent.

Biggs argues that the state must take risks to earn that high a rate, while the pension obligation will be the same whether the markets soar or crash. He says states should use a risk-free rate, perhaps something closer to the 2.8 percent that Missouri pays on 15-year bonds. His study uses 4 percent, which he says "might be thought of as approximating rates over a longer period of time."

A lower discount rate means a bigger future liability. Most academic economists would agree with Biggs' argument, but Steve Yoakum, executive director of the Public School Retirement System of Missouri, says it doesn't work "out here in the real world where I have to live."

He says the PSRS fund, which assumes that it will earn 8 percent returns in the future, has actually earned 9.3 percent on average over the past 20 years. "For us to make an assumption that we're not going to do that in the future would be kind of foolish," he said.

Gary Findlay, executive director of the Missouri State Employees Retirement System, argues that Biggs' "fundamental flaw" is "the presumption that public sector defined benefit plans should be in the risk elimination business rather than the risk management business."

Using a risk-free discount rate, Findlay says, is about as sensible as arguing that the state should take a zero-risk approach to traffic accidents — by banning cars.

Findlay and Yoakum argue that Biggs and the Show-Me Institute approached this study with an agenda: promoting 401(k)-like plans as a replacement for traditional defined-benefit pensions.

Biggs does indeed argue that a defined-contribution plan, like a 401(k), would limit future liabilities and would be "superior … in terms of attracting and retaining quality employees."

He may be right. Many private employers say young workers are much more interested in a good 401(k) than in a pension that they may not stay around long enough to collect.

The state's pension managers would counter that they've created a lot of value for public employees, and they're right. Taxpayers, however, could benefit from a full-fledged discussion of the costs, benefits and risks of maintaining the pension system.

House, Senate at odds over potential pension reform

By Kathleen Haughney, Tallahassee Bureau, March 24, 2013

The Florida House is moving to shutter the state's pension system and send all new employees to a 401(k)-style option, but the plan is running into stiff opposition from a more-moderate Senate and union groups who say that the proposal would be a raw deal for public employees.

"I think it would be a cold day before we would change our position on this bill," said Sen. Wilton Simpson, R-Trilby, who is the Senate's point man on reforming the state pension system.

The House on Friday voted 73-43 on its proposal, HB 7011, to require new public employees — including teachers, police, firefighters and all state workers — to enroll in an investment plan starting in 2014.

Critics say that means future pension benefits would depend on the performance of the stock market. By contrast, the state's current defined-benefit plan pays a guaranteed amount based on a worker's salary and years of employment.

But House members, led by Speaker Will Weatherford, R-Wesley Chapel, cite such states as Illinois that must spend billions of tax dollars to shore up underfinanced pension funds. And though Florida's $128 billion fund is considered healthy — able to fund 87 percent of its future obligations — they say it could go south in a hurry.

"The worse the economy gets, the higher the potential cost," said state Rep. Dana Young, R-Tampa.

They also note that most private businesses have closed their pension plans in favor of 401(k)s to eliminate any future liabilities for their workforce.

The House has argued that shifting to the investment-plan strategy would save the state billions. A study requested by Weatherford reported that the state could save $9.8 billion over 30 years.

But the public-employee unions that represent teachers, police officers, firefighters and other state employees are strongly opposed. The reason? In down markets, investment plans perform poorly.

The state has allowed employees to choose between "defined benefit" and investment or "defined contribution" plans for the past decade. Of the current 623,011 employees and 334,682 retirees covered by the Florida Retirement System, 75 percent are in the defined-benefit system.

According to the state, over 10 years, the pension system has outperformed the individual investment plans by 1.07 percentage points. The pension system's one-year-return rate also bested the individual investment plan by 3.69 percentage points. Over a 20- or 30-year career, pension proponents argue, that difference can mean substantial dollars.

"These changes leave the possibility for teachers and other public servants will have to work past the age of retirement, if they can afford to retire at all," said Florida Education Association President Andy Ford.

House Democrats also argued that public employees might be choosing public service — and potentially a lower salary — because of the potential of a guaranteed retirement fund. State employees have not seen a pay raise in six years.

"Go pick someone else's pocket and leave our public servants alone," said state Rep. Irv Slosberg, D-Boca Raton.

The Senate is pursuing a far different approach.

Its proposal would let new employees choose between an investment and defined-benefit system, as now. But unless they affirmatively opted for defined benefits, they'd automatically be put in an investment plan. A few categories of employees — notably senior management and lawmakers — would be required to choose the investment plan.

Proponents say it makes sense for people who don't plan a career in public employment to opt for investment plans because they are "portable" and can be rolled into a new 401(k) account once the employee leaves. By contrast, employees who quit after a few years would leave their defined-benefit plan benefits behind.

State Sen. Jack Latvala, R-Clearwater, a leading member of the Senate, said during a recent committee debate that the Senate needed to fight the House on its "broad-brush" proposal.

"I think it's wrong," he said. "It's ill-conceived."

This isn't the first time the Legislature has moved to overhaul the state's retirement system. In 2011, legislators made several changes, including one that required employees to contribute 3 percent of their salaries to their retirement. Previously, they had contributed nothing.

Kansas lawmakers end push for 401(k)-style public pension plan

By JOHN HANNA, The Associated Press Posted on Thu, Mar. 21, 2013

A proposal for issuing $1.5 billion in bonds to boost the long-term health of Kansas' public pension system advanced Thursday in the state Legislature, but Republican lawmakers who want to put new government employees into a 401(k)-style plan abandoned an effort to pass such a bill this year.

The GOP-controlled House Pensions and Benefits Committee approved a bill authorizing the bonds on a 7-6 vote, sending it to the entire House for debate. But on a voice vote, it tabled a separate measure to start the 401(k)-style plan for state and local government workers hired after 2014, as well as a separate, non-traditional plan for new teachers.

The measures followed two years' worth of legislation overhauling the retirement system for teachers and state and local government employees. The committee faced skepticism from retiree groups and public employee unions that lawmakers needed to consider additional changes this year.

The Kansas Public Employees Retirement System projects that previous changes – which include boosting state contributions and setting aside state casino profits to pensions – would eliminate a projected $9.3 billion gap between revenues and benefits promised to workers by 2033. But many GOP lawmakers believe such a gap will occur again if the state isn't more aggressive in moving away from traditional plans that guarantee benefits upfront, based on a worker's salary and years of service.

“They look at it and say, `Why would you ever want to put the state in that position?“' said committee Chairman Steve Johnson, an Assaria Republican.

The bill authorizing bonds is designed to give KPERS a quick infusion of cash, so that the percentage of its obligations covered by its assets, now 53 percent, would jump to 61 percent in 2015 and grow more quickly than it would under current law. Also, the state wouldn't have to boost its annual contributions to KPERS as aggressively.

Both Republicans and Democrats were split over how much financial risk the move involves and whether it does enough to improve the retirement system's financial footing.

Putting new government workers into a 401(k)-style plan would base their retirement benefits on investment earnings. In their new plan, teachers would contribute part of their salaries to tax-free annuities paying out once they retired, with multiple options for the riskiness and potential benefits from their investments.

Public employee and retiree groups believe all of the potential options will result in less secure pensions because of the potential volatility of financial markets.

Lisa Ochs, president of the Kansas chapter of the American Federation of Teachers, said legislators have studied such changes in depth and concluded previously that they come with costs while sacrificing benefits.

“We have an obligation to each other in a civilized society to make sure that we're doing what we can to make sure that our public servants have a retirement they can depend on, have a dignified retirement and that we're not creating generations of indigent elderly,” she said.

Most committee members said they needed more time to consider the bill. Lawmakers expect to wrap up most of their work for the year on April 5, and tabling the pensions measure means they won't consider it until next year.

“We just don't have the time to really spend another month, basically, to come up with the best plan,” said Rep. Jim Howell, a Derby Republican and the committee's vice chairman. “I do agree that this is the right thing to do today, but we've got to get back into it.”

Republican legislators and GOP Gov. Sam Brownback's administration worked quietly for weeks on the measure for a 401(k)-style plan. They unveiled it with a big splash this week in a hearing featuring Nobel Prize winner Robert Merton and Bill Bradley, the former Democratic presidential candidate and U.S. senator from New Jersey who also used to be a New York Knicks standout.

Both Bradley and Merton, a finance professor at the Massachusetts Institute of Technology, advise an Austin, Texas, company that manages private-sector 401(k) plans. The measure called for having private companies manage the new plans.

Pension Reform Success Stories

Most states and many municipalities have passed some kind of pension reform in recent years, but only a few did so in a way that addresses the immediate unfunded liability of their plans.

BY: Liz Farmer | April 2013

For Chris Bartley, the turning point in Lexington, Ky.’s pension deal came when the city finally budged. The longtime firefighter and union chief was slow to trust politicians. So he stood his ground and well into fall 2012, Bartley and other representatives returned again and again to the negotiating table. Tasked with fixing the city’s looming pension debt created by slow revenue growth and soaring entitlement costs, they had made no progress.

Then it happened, Bartley recalls. The city said it had come up with a way to increase its pension funding -- and could guarantee those payments. It was the first step in a compromise deal that city officials today believe will make the fund solvent.

“Somebody had to step first,” Bartley remembers. “They moved, and it allowed us to make some movement.”

As in Lexington, many state and local pension plans are in crisis. Thanks to the recession’s toll on pension portfolio returns and its pressure on budgets, many public pension plans at both the state and local level have become woefully underfunded -- threatening future benefits. Meanwhile, the tight budget climate has strained relations between employee unions and employers, making it difficult to pass meaningful changes that would assure employees of their full retirement benefits and keep pension systems current with state and local revenue.

Most states and many municipalities have passed some kind of pension reform in recent years, but a smaller number have been able to do so in a way that addresses the immediate unfunded liability of their plans. Both sides have shirked responsibility, says Elizabeth Kellar, president and CEO of the Center for State and Local Government Excellence. “Neither the management side nor the labor side has owned up to reality.”

Now there will be new factors. The Governmental Accounting Standards Board rules set to kick in this summer will change the way public pension plans account for their portfolio gains and losses. That will likely have the effect of making a plan’s unfunded liability appear higher than it did in prior years. Coupled with announcements from credit ratings agencies that they will downgrade states with high unfunded liabilities, the pressure on public pension reform is mounting.

Some pension plans, however, have tackled those pressures successfully. While the processes vary, the themes for progress are consistent: education, reciprocity and trust. While it may seem essentially a public relations campaign to engage employees and inform the public, it is by no means a simple road to meaningful reform. It can, however, be worth the effort.

One person who took the education component seriously is San Jose, Calif., Councilman Pete Constant. A former cop, Constant was elected to the council in 2006 and by 2012, pension costs had grown to 27 percent of the city's general fund budget. Constant made it his mission to understand exactly how pensions work or don't work and took courses at the University of Pennsylvania, University of Chicago and Stanford Law School. (He's now on his way to finishing his doctorate in public pension governance.) He's used his expertise to launch a pension education crusade of sorts, making the case to voters and his colleagues that San Jose's system was broken.

"What I took on as a personal challenge is, how can I learn these complex concepts and present them in ways simple enough to make people understand?" says Constant. In coordination with Mayor Chuck Reed and others, officials spent nearly three years discussing the city's pension problem in public forums before proposing changes to the system that targeted retirement age and restructured employee contributions. "Once people start to connect the dots, you see the light go [on]," Constant says of the forums. Last June, voters overwhelmingly approved changes that included raising the retirement age to 65 for most employees; requiring current employees to contribute an additional 4 percent of their salaries or switch to a lower-cost plan; and allowing the city to suspend cost-of-living adjustments (COLA).

But San Jose's method largely bypassed the unions, and now the city is embroiled in a costly -- albeit expected -- lawsuit.

Educating the voters *and* public employees on what's wrong with the current system would seem to be key. It's also extremely difficult.

"People's eyes glaze over," says Fitchburg, Mass., Mayor Lisa Wong. After redesigning health-care coverage for current and future employees and retirees, which reduced other post-employment benefits costs and addressed roughly 40 percent of the city's unfunded liability, she has now made changing the pension plan itself a top priority this term. Accordingly, she has assembled a public employee committee with representatives from each of the city's 16 unions. "One of the solutions [I've used] in terms of discussing it publicly is talking about this issue of trade-off," she says. "People want to know why, if their taxes are going up and services going down, this is happening. And I had to say because we trade off current services to pay for past bills. That's a very difficult conversation to have."

It's a conversation that Rhode Island Treasurer Gina Raimondo had dozens of times with taxpayers and state employees as she launched her tour around the state to advocate for pension reform in 2011. "Often these meetings would last for hours," Raimondo says, adding, "Public employees did nothing wrong. They did what they were told -- it was the system that was poorly designed."

At the meetings, Raimondo would talk to employees, telling them, "I'm sorry, I have a tough message. But I'm here to work with you." Raimondo says attendees would often start off angry but by the end, thanked her. "They said I was the first person to lay it out like that for them."

That year, she persuaded the Democrat-controlled legislature to pass pension changes that she projects will save up to $4 billion by delaying retirement, suspending COLAs and changing existing and new workers' plans to a hybrid pension/401(k)-style plan. Still, Rhode Island's legislation never won union support and now faces a legal battle.

Part of unions' stiff opposition to pension changes can be traced to a lack of trust in the numbers pension sponsors' report. Indeed, for every state chart that shows a less-than-expected rate of return on pension investments over the last decade, pro-union groups have their own or independent studies that show better rates of return over 20 or 30 years. "It's disingenuous at best to say they're on an education campaign," says Jordan Marks, executive director of the National Public Pension Coalition. He rejects the picture that politicians present of reduced services versus pension cuts. "It's a false choice," he says. "Smaller class sizes or teacher pensions? It's not one or the other -- budgets are made up of thousands of decisions."

Marks says the lack of fairness has created distrust among workers. It runs deeper than disputes over rates of return on portfolios. Many states and localities have not paid in their required contributions in recent years as budgets have become strapped. (Rhode Island, Raimondo notes, has made its payments.) And employees -- who have also dealt with salary freezes -- have no control over how much they contribute to their pensions. The system has left a sour taste in the mouths of current public employees who now view pension reform as a bailout to states using their hard-earned money.

Melissa Turner, 34, is one such employee who feels she was given a "bait-and-switch" after 12 years at the University of California at Davis. Several years ago, her retirement benefits changed. That means she will have to work for the university 15 years longer -- until she is 65 years old -- to receive what was originally laid out for her. Meanwhile, budget cuts have allotted her just three raises in 12 years averaging less than 2 percent while her pension contribution percentage has more than doubled. The changes have disabused her of the notion that her job as a construction project coordinator will provide retirement security. "Let's face it, the system our parents grew up on is not going to be the same system that's there for us," she says.

Overcoming that broken trust can mean that pension reform doesn't have to be mandated from on high, but reciprocity is an absolute requirement. Lexington Mayor Jim Gray believes he's done just that with reform the city passed in January and has since been approved by the state legislature. Put together by a pension task force made up of city officials, union representatives like Bartley and the aid of an outside financial consulting firm, the measure guarantees that Lexington will increase its annual contribution to the pension fund to $29 million from $11 million. At the same time, employees have agreed to an older retirement age and increased contributions.

Both sides say hiring a financial consultant with no ties to the city helped keep everyone in line and bring about compromise after months of standstill. "We just laid everything on the table -- nothing would be held against each other," Bartley says, "and before long, we were making progress."

Gray adds that the environment created a sense of common purpose and shared sacrifice. "That language can sort of sound artificial, cliché, sanitized and all sugar and spice," he says. "But getting to that level of trust was hard work. Patience and persistence were required and a willingness to just stay at the table."

Employees can be an asset and resource when it comes to redesigning pensions, says Ken Parker, former city manager of Port Orange, Fla. Including them in the redesign is likely to take longer than officials probably prefer. But after five years of efforts from city officials, Parker says Port Orange now has a sustainable pension plan. The city was able to reduce the benefits for current firefighters while the union got its wish for more money in the budget for new hires.

“Sometimes we assume that they don’t want … to be a part of the solution, which, in fact, I think they do,” Parker says. “By engaging the employees, you come up with better solutions than you do if you’re trying to mandate them.”

Launching a PR push on pension reform doesn’t guarantee success; only time will tell whether the changes enacted today will work for the years ahead. Nearly two years after Atlanta became the first city to pass major pension reform upping employee contributions and reducing COLAs, Mayor Kasim Reed says the city is saving at least $25 million a year.

The wave of reforms following Atlanta and Rhode Island’s changes signals a growing acceptance that, in many cases, the current system can’t last. In some places that has created a blame game that’s inhibiting compromise. In Illinois, employees point out that their state has been woefully derelict in paying into the plan, which is roughly 40 percent funded. Illinois’ inability to address its unfunded liability was a major factor in its recent downgrade by Standard and Poor’s. Last month the Securities and Exchange Commission charged Illinois with securities fraud for misleading investors about the health of its pension program.

St. Paul, Duluth teachers pension fund bailout OK'd by commission

By MaryJo Webster, mwebster@pioneerpress.com, Posted: 04/02/2013 12:01:00 AM CDT

A bill to provide $7 million in annual state aid to a pension fund for teachers in the St. Paul School District will move to the full Legislature.

Lawmakers on the Legislative Commission for Pensions and Retirement voted 10 to 4 to advance the bill Tuesday, April 2. Along with the aid, the bill also includes increased contributions and cost-saving measures in an effort to close the retirement fund's $16.7 million annual gap between what it needs and what it brings in.

The commission also approved a similar measure that includes $6 million in annual state aid for the Duluth Teachers Retirement Fund Association and approved a Teachers Retirement Association proposal to change early retirement benefit reductions in an effort to encourage teachers to keep working until at least age 62.

The group also signed off on an omnibus bill that includes fixes for the pension funds for judges, police officers and firefighters, state troopers and other state public safety employees. Those bills also move on to the full Legislature.

The proposals to stabilize the St. Paul Teachers Retirement Association Fund and the Duluth pension were among the most controversial issues the commission discussed this session. At the forefront of the discussion was the issue of whether the two plans should be merged into the statewide Teachers Retirement Association.

Rep. Mike Benson, R-Rochester, asked that merger discussions, particularly regarding the Duluth fund, continue after the legislative session. "It's not so much that I don't believe you need help," Benson told representatives from the Duluth pension."I'm not so sure that it's best to rush."

Commission chair Sen. Sandra appas, DFL-Minneapolis, noted that the statewide TRA would require Duluth and St. Paul plans to be fully funded before any merger.

"This is a kind of shared-pain approach," Pappas said of the St. Paul proposal. "If we're thinking merger is down the road, bringing benefits in line with TRA and putting some cash into the fund is probably a good move."

St. Paul's proposal calls for about $7 million per year in state aid until the plan reaches full funding, which is expected to take 25 years. It also increases employee and employer contributions and makes retiring early and returning to work after retirement less attractive. The multiplier to calculate benefits would also be increased to match what TRA offers.

The fund currently has assets to cover only 63 percent of its liabilities. Without the fixes included in this proposal, the pension plan is expected to sink to 38 percent funded by 2036. With the fixes, it could reach 80 percent funded in less than 20 years.

Paul Doane, the fund's executive director, said the proposal is a "very fair and balanced approach" to the fund's financial problems, which largely stem from years of underfunding.

The Duluth pension fund is characterized as being in a "seriously weak actuarial condition," largely because it has more retired members than working members. The bill approved Tuesday calls for $6 million in state aid, increased employer and employee contributions, 1 percent cost-of-living adjustments for retirees and increasing the benefit formula to bring it in line with TRA.

Tom Threinen, a retired elementary school principal from Duluth, told lawmakers the additional contribution costs for the Duluth school district will result in the loss of at least five teaching positions and make it harder for the district to reduce class sizes and increase offerings, which parents are clamoring for.

"The pension fund problem is a real one, but it's one we as adults created, and it's wrong to solve that problem on the backs of kids in Duluth," Threinen said.

Threinen also urged the commission members to study the bigger issue of the state's $16 billion in unfunded pension liabilities.

"The longer we wait, the larger the problem will become and more distasteful the choices will become," Threinen said.

Educator pension fix signed into law

By James Monteleone / Journal Staff Writer

Teachers and taxpayers will pay more into the state educators' pension system under the plan to shore up the struggling fund approved Friday by Gov. Susana Martinez.

The solvency measure, passed earlier by the Legislature, is intended to restore the New Mexico Educational Retirement Board pension plan to be 100 percent funded by 2043.

Changes affect nearly 61,000 active state teachers and educators who contribute to the pension plan and about 37,000 retirees receiving benefits.

The approved ERB fix taking effect July 1 will:

♦ Increase taxpayer contributions to 13.15 percent of all employee wages starting in July, up from 10.9 percent. Taxpayer contributions increase again next year to 13.9 percent. The taxpayer increase matches the level set by the Legislature in 2005 but was delayed because of lean budget years.

♦ Increase employees' contributions to 10.1 percent, up from 9.4 percent. Employee contributions increase again next year to 10.7 percent. Employees earning less than $20,000 per year will contribute 7.9 percent of their wages.

♦ Reduce current retirees' annual cost-of-living benefit raises to 1.8 percent per year — a 10 percent cut— for educators with 25 years of services and 1.6 percent per year — a 20 percent cut — for all others.

♦ Change rules for new hires by setting a minimum retirement age of 55 and delaying cost-of-living benefit increases until age 67.

The governor said the changes are an important step toward shoring up the estimated $6.2 billion unfunded liability of the educators' pension plan that is now about 60 percent funded.

"This proposal represents systemic reform to the state's educator pension system," Martinez said. "Our negotiations with the Legislature resulted in several concessions and improvements to bolster the system's long-term solvency and moved us toward our ultimate goal of saving more than $6 billion over the next three decades."

Martinez said she would continue to work with lawmakers to ensure the educators' pension plan remains on track to solvency.

The intended fix for the educators pension system comes after years of meetings with teachers, retirees and state leaders to identify the best solution, said Jan Goodwin, executive director of the Educational Retirement Board.

"Everyone worked together through thick and thin, adapted to any changes that were put before them, and they stuck together and got something that worked for the governor," Goodwin said Friday after the legislation was signed into law.

“What a huge feeling of relief,” she said.

But the signing of the legislation also came after the pension plan fix drew fire from both liberal and conservative quarters.

Some progressive Democrats argued the plan was unfair to retired teachers, who are facing decreased cost-of-living raises not being cut from other public employees.

“The Legislature and the executive, they just have no regard for teachers by doing that,” said Rep. Mimi Stewart, a Democratic Albuquerque educator who voiced opposition. “… Why are we holding the ERB fund at a higher standard?”

If the fund were to reach 90 percent funded status, it would trigger a restoration of slightly higher cost-of-living raises.

Other critics had said the plan didn’t go far enough to reach solvency.

Educational Retirement Board member Bradley Day in a Journal op-ed called the fix “inadequate” and said the pension benefits were too generous for the contributions employees paid.

Most educators covered by the ERB must work for at least 25 years to be eligible for full retirement benefits, though there is no current minimum retirement age. Benefits are calculated through a formula that includes an employee’s final average salary and number of years worked.

Other legislation designed to improve funding for the state’s other large public pension system, the Public Employees Retirement Association, still is being reviewed by the governor, Martinez spokesman Enrique Knell said.

States move along different roads to tackle underfunding dilemma

By: Melanie Zanona

More states are enacting measures to help improve the solvency of their public pension funds as funding ratios remain low.

While pension reform is not a new phenomenon — 43 states enacted retirement plan changes between 2009 and 2011, according to the National Conference of State Legislatures — states are taking different paths, including efforts to move to cash balance plans, alter cost-of-living adjustments or shore up funds through alternative revenue sources.

“There's been a lot (of pension reform) on the table and every state has approached this differently,” said Chris Mier, managing director at Chicago-based Loop Capital Markets LLC, an investment services firm that tracks public pension funding every year. “I think 30 states are in roughly good shape, but there are probably five that need to get going. I don't view this as a systemic problem; I view this as a state problem.”

Among the entities making changes this year are Kentucky, Puerto Rico, Florida, Kansas and Maryland.

Kentucky, which has about $18 billion in unfunded public pension liabilities, passed legislation on March 26 that will develop a cash balance plan for state and local employees hired on or after Jan. 1, 2014. Under the new plan, employees also will be able to purchase an annuity or receive a lump-sum payment on retirement.

“The most significant reason for passing the legislation was to address the underfunding problem in at least two of the plans we administer,” said William Thielen, executive director of the Kentucky Retirement Systems, Frankfort, which oversees the state's five pension plans with $10.9 billion in assets. “For 14 out of the last 21 years, (the Kentucky General Assembly) has not put in the actuarially required contributions.”

The two most underfunded of the state's plans are the Kentucky Employees Retirement System (non-hazardous plan), which was 27.3% funded as of June 30, 2012, with $11 billion in liabilities and $3 billion in assets; while the Kentucky State Police Retirement System was 40.1% funded as of the same date, with $648 million in liabilities and $260 million in assets.

The law will generate the $100 million a year needed to fully cover actuarially required contributions through changes in the tax code and reducing the personal tax credit by $10.

Another provision of the law requires a cost-of-living adjustment to be fully prefunded by the General Assembly in the year it is provided, which “essentially eliminates” them, according to Mr. Thielen.

“It's not something that was desired from the standpoint of retirees, but I think everyone realized the necessity,” he said.

According to Loop Capital's annual Public Pension Funding Review, the changes to defined benefit plans that are met with the highest level of opposition from employees and retirees are eliminating the COLA and moving to a cash balance plan, followed by increasing the retirement age, increasing contribution rates, and reducing disability and death benefits. But Mr. Mier said the most controversial changes can sometimes be the most effective, too.

“The trade-off you face is, "Do I want to solve the problem in the shorter term or the longer term?'” Mr. Mier said. “Migrating to a DC plan doesn't give you an upfront benefit, but it gradually happens.”

Puerto Rico opted to overhaul its cash-strapped public pension fund by keeping the defined benefit plan but making significant changes to funding requirements and retirement age.

The law, effective July 1, 2013, will increase employee contributions to 10% from 8.275% of pay, increase the retirement age for some workers, and lower future monthly pensions and benefits.

Puerto Rico downgraded

The Puerto Rico Employees Retirement System, San Juan, has a funding ratio of 6.8%. That, coupled with the government's budget deficits, led to the downgrading of Puerto Rico's bond ratings to just above junk-bond status by all three major credit ratings agencies.

At the other end of the scale, pending legislation in Florida would close the Florida Retirement System's defined benefit plan to some employees and move all new employees to a 401(a) plan. The legislation was voted out of committee and is scheduled to go before the full Senate the week of April 15.

The measure would also offer an incentive for current employees to enroll in the 401(a) plan by reducing required contributions to 2% from 3% of pay, and requiring the state to contribute an extra 1%. The vesting period for the DB plan, also would be increased to 10 years from eight years.

Instead of making direct changes to the Kansas Public Employees Retirement System, the state is trying to shore up the fund through alternative methods.

A bill will be taken up by the full state Senate on May 8 that would allow Kansas to borrow $1.5 billion, through the sale of taxable bonds, to help fund pension obligations.

This is not the first time the state has generated revenue for pension relief: last year, Kansas used $47 million in casino proceeds to help fund its ailing pension system.

The funding ratio was 59% with $9.2 billion in unfunded liabilities as of Dec. 31, 2011.

Maryland recently passed a law that would change the way contribution rates are calculated.

Last week, the Maryland General Assembly passed and sent to the governor for signature a bill that would gradually eliminate the current "corridor method" of funding the $40.2 billion Maryland State Retirement and Pension System. Under these calculations, which were adopted in 2002, Maryland could maintain its contribution rate from the previous year as long as the funding ratio remained between 90% and 110%. If the funding ratio dipped below 90%, the contribution rate would equal the previous year's rate plus 20% of the difference between the actuarially required contribution and the previous year's rate.

The new measure would allow Maryland to contribute $19 million less in fiscal year 2015 and save the state an estimated $450 million once the corridor method is completely phased out by 2024.

The bill also eliminates a tiered amortization period and replaces it with a closed, 25-year amortization.

The funded status of the six pension funds in the Maryland system was a combined 64.4% as of June 30. Only the $329 million judges' pension fund was more than 70% funded, at 78.4%.

"The Legislature has taken a very important step in eliminating a funding method that has contributed to an underfunding of the system," Nancy K. Kopp, state treasurer and chair of the pension system board of trustees, said in a statement. "

Some efforts have stalled

But not every pension reform plan meets with success.

Pennsylvania Gov. Tom Corbett put a pension reform plan in his 2014 fiscal budget in the beginning of year, but so far no legislation has been proposed. Mr. Corbett's plan would cut future benefits for current employees and move new hires into a defined contribution plan.

Illinois, despite having the worst-funded state pension plans in the country with a combined $97 billion in unfunded liabilities, has remained in political gridlock and not passed any comprehensive reform, even though several measures have been taken up by the Legislature.

"There's kind of a correlation between the size of the problem and the degree of political difficulty of instituting a solution," Mr. Mier said. "The political problems enable the pension problem to get bigger, and vice versa."

Minnesota public pensions are unique

- Article by: Mary Vanek, Dave Bergstrom and Laurie Hacking , April 11, 2013 - 9:08 PM

Counterpoint

A favorite pastime of public-pension opponents is comparing Minnesota to states with big pension problems, such as California ("Minnesotans may be in for a rude surprise," April 5). This comparison just doesn't fly.

Minnesota differs from California in several ways. Minnesota passed bipartisan pension reform legislation in 2010 that required significant shared sacrifice from retirees, active public workers and public employers and that has been cited as a model for other states. Public workers have always contributed roughly half the pension cost in Minnesota, and in fact, 80 percent of the solution to our funding problems in 2010 came on the backs of public employees through benefit cuts and higher contributions.

In Minnesota, worker contributions have always been higher than average and public employer contributions lower. The average employee pension payroll deduction in Minnesota is about 6 percent. The national average is about 5 percent. The average public employer contribution (the taxpayer portion) in Minnesota is about 6 percent, compared with a national average of 10.3 percent. Employer/taxpayer costs are only 1.6 percent of state and local government spending here, compared with 2.9 percent in other states, according to the U.S. Census Bureau.

So it is misleading for Kim Crockett of the Center of the American Experiment to use other states as indicative of what is happening in Minnesota. The Minnesota Legislature has a long history of handling pension obligations in a responsible manner. The 2010 reforms, combined with improved investment returns, have lowered the public pension systems' unfunded liabilities by more than $10 billion since 2009 — and will continue to generate savings going forward.

Bills under consideration at the Legislature will improve the funds' status even more. Changes to the Public Employees Retirement Association Police and Fire plan will cut benefits by $458 million. Both retirees and active members are being asked to make sacrifices, with 78 percent of the solution to the plan's financing problems being shouldered by public workers. Similarly, changes to the Minnesota State Retirement System State Patrol and Judges plans will reduce benefits by $35 million.

But antipension lobbyists have a bigger agenda: to get public employees shifted into a 401(k)-type retirement plan — the same type of plan that is failing private-sector workers.

Taxpayers should be wary. First, when a public pension plan is closed and contributions are siphoned into private accounts, the taxpayer is on the hook for the costs of meeting the obligations of the existing pension plan. The Minnesota retirement systems' actuary estimated that the state would incur transition costs of about $3 billion over the next 10 years if the defined-benefit plans were closed. The scenario would be similar to what happened after the Minneapolis Police and Fire plan was closed to new members in 1980 and after the Minneapolis Employees Retirement Fund was closed in 1978. Only much bigger.

Second, taxpayer costs would shift to the areas of state government that deal with poverty: public assistance and nursing home costs. The retirement crisis in this country is in full swing, with far too many Americans hitting their retirement years and finding that their 401(k) savings are nowhere near enough to sustain them as they age. Those who are able to continue working are doing so. Those who are not must try to make ends meet on Social Security. If they can't, they turn to taxpayer-funded public assistance.

We need to ask ourselves some tough questions. Do we want to make a half-million Minnesota public employees less income-secure in retirement? How will that benefit our state? How does it benefit private-sector workers if we throw Minnesota's public employees into a flawed, inadequate retirement system such as the 401(k)?

Minnesotans deserve less free-floating panic and more focus on the big picture and what kind of state we want to live in.

Protect Pennsylvania pensions

April 18, 2013 12:17 am, by Diane Oakley

Pennsylvania taxpayers want reliable public services delivered at a reasonable cost. These public services are provided by trained and experienced Pennsylvanians such as teachers, nurses, paramedics and park foresters. But it's an ongoing challenge for public employers to recruit and retain highly qualified workers to deliver these services.

Government employers have significant disadvantages when recruiting employees. They cannot offer higher salaries typically offered to professionals and managers in the private sector. For example, more than half of public employees in Pennsylvania have a college education, yet data indicate that these highly qualified public employees earn 21 percent less on average than comparably educated private sector employees. In similar comparisons across all workers, public sector pay trails private sector pay by 11 percent to 12 percent.

One management tool that helps public employers stabilize a large workforce is the ability to offer good retirement benefits. Pensions that pay a monthly benefit check based on employee's years of service enable the state of Pennsylvania, for instance, to recruit and retain high quality workers. Because pension contributions are a shared responsibility among employees and employers over the long term, investment earnings pay most of the cost of the benefits. As Eli Leher of the conservative Heartland Institute indicates, public employers "have a strong comparative advantage relative to private industry in offering pension benefits."

The Pennsylvania Legislature is considering a proposal to dismantle the pension system provided to public employees in Pennsylvania in favor of individual 401(k)-type accounts. Not only would this change undermine the ability of middle-class Pennsylvanians to be self-sufficient in retirement, it would threaten the quality of education and public services in the state by making it even harder to keep qualified and experienced employees.

Towers Watson research finds the percentage of workers under age 40 who agree that a pension plan is important in their job choices has soared -- to 63 percent in 2011 from 28 percent in 2009. Pensions also land near the top of workers' "top ten" list of benefits, while 401(k)-type savings plans rank near the bottom. More than three-fourths of new hires say their defined-benefit pension gives them a compelling reason to stay at a job, reducing employee turnover that undercuts productivity.

The financial crisis provided a key lesson about the economic value of pensions. Spending by retirees with predictable pension checks stabilized the struggling U.S. and commonwealth economies. In 2009, retired public employees in Pennsylvania continued to spend their monthly incomes at grocery stores, pharmacies and local restaurants. This cash flowing to private businesses from Philadelphia to Pittsburgh supported nearly 100,000 jobs and $14 billion in economic output. In contrast, retirees with plummeting 401(k) accounts scaled back spending when the economy most needed it.

More than 70 percent of Americans agree that the public sector employees who protect and shape our future should receive a pension. So it is not a surprise that, after the financial crisis, Pennsylvania and nearly every state enacted changes to their public pensions to ensure long-term sustainability and maintain this vital human-resource tool.

Pennsylvania's 2010 Pension Reform Act cut pension benefits for new employees by over 20 percent, reducing employer cost of future pensions to only 3 percent of salaries. Meanwhile, school and state employees contribute more -- 7 percent on average from every paycheck -- to fund their pensions. The Legislature in 2010 also committed to restoring proper funding, correcting for the diversion of pension contributions to other purposes over the last decade. Over time, the 2010 changes will restore Pennsylvania's public pensions to full funding.

Now, lawmakers are considering replacing the pension plan for new employees with a 401(k)-type plan. In addition to making it more difficult to hire and retain first-rate employees, such a path, according to a wide body of research and employer experience, is ill-advised because:

• Closing an existing pension plan to new employees means fewer employees share the cost of existing pension commitments, leaving taxpayers on the hook to make up any difference.

• Switching to 401(k)-type individual accounts would cut retirement income beyond the 2010 reform, leaving Pennsylvania's public servants less able to support themselves in retirement after a career working for the public good.

• Taxpayers would lose the significant cost efficiencies of lower fees and better investment returns achieved by defined-benefit pensions in a switch to 401(k)-type individual retirement accounts.

The workforce and economic benefits of pensions are key factors to consider while examining pension proposals that would undo the 2010 reforms. Experts agree that the 2010 changes will work over time -- if everyone does their fair share.

Given the anxiety 85 percent of Americans feel about retirement, it's no wonder that a similar percentage agree that all workers should have a pension so they can be independent and self-reliant. Real pension reform for Americans should start with better retirement security for all.

Diane Oakley is executive director of the National Institute on Retirement Security.

Fix for teacher pension fund advances in Nebraska Legislature

By Paul Hammel, WORLD-HERALD BUREAU

LINCOLN — Teachers in Omaha and elsewhere in the state will pay a little more toward retirement, and the state will contribute more, as part of a legislative solution to a state pension shortfall advanced Thursday.

The economic downturn that began in 2008 left Nebraska with a $108 million shortfall in the state pension plans for Omaha teachers and teachers statewide.

Thursday, state lawmakers gave initial approval to a measure that would close that gap, Legislative Bill 553.

The 33-0 vote came after State Sen. Jeremy Nordquist of Omaha, chairman of the Legislature's Retirement Systems Committee, answered several concerns from colleagues about the sustainability of the plan.

Senators questioned whether Nebraska ought to consider moving away from a defined benefit pension plan for teachers.

Defined benefit plans are similar to Social Security, in that they ensure a constant benefit upon retirement. Employers, as well as employees, might have to adjust their contributions if investment returns are inadequate to maintain benefits.

Defined contribution plans, meanwhile, are similar to 401(k) plans. Retirees get only what the return is on their pension investments; less if the investments do poorly and more if they do well.

Nordquist said that switching to a defined contribution plan or a hybrid "cash balance" plan would cost the state many more millions of dollars than LB 553.

A switch, he said, would leave the state with a huge pension liability because new employees would no longer contribute to maintain fund balances for those on the defined benefit pension plan.

Omaha Sen. Heath Mello, who is chairman of the budget-writing Appropriations Committee and sits on the Retirement Committee, said switching plans would require a one-time allocation of from $400 million to $500 million.

"We don't have the money to do that. It's not fiscally responsible, and it's not a fiscal reality."

LB 553 was merged with LB 554, a bill dealing with the Omaha teachers pension plan. LB 553 requires:

» All school employees would continue to contribute 9.78 percent of their pay toward retirement. That figure had been scheduled to drop to 7.28 percent, the rate prior to 2011. It was increased to address a short-term funding problem raised by the recession.

» School districts will continue to contribute 101 percent of what employees contribute.

» The state would increase its contribution from 1 percent of compensation to 2 percent, which translates to about $20 million more a year.

» Future teachers' cost-of-living increases would be capped at 1 percent. For current teachers, the rate is 2.5 percent. Future teachers' pension checks would use five years' of wages to compute a final average salary, rather than three. That change will reduce benefits.

» Employees would have to work 20 hours a week, instead of the current 15 hours, to qualify for the pension plan.

Nordquist said that a good pension plan helps retain quality teachers and that in recent years, teachers and school districts have contributed 90 percent of the funds to shore up the plan.

Now, the senator said, it's the state's turn.

“Everyone steps up,” he said, under LB 533.

Columbus Sen. Paul Schumacher questioned whether the assumption of an 8 percent annual return on investments was realistic, given the recent economic downturn.

He also asked whether lawmakers would have to patch up the pension system again in a couple of years.

“This is just the leading edge of a massive problem,” Schumacher said. “Baby boomers, grab your behinds, because this is going to be a rough ride.”

Nordquist said he understood the senator's concern but said the state must operate on the best assumptions it can.

He noted that a state investment board is weighing whether to lower the assumption from 8 percent.

Contact the writer: 402-473-9584, paul.hammel@owh.com

Adjustable pension plan design begins to gain converts

By: Kevin Olsen , Published: April 29, 2013

A new pension plan design that allows employers to drastically reduce their risk while still providing lifetime income to participants is gaining support as an alternative to moving employees into a defined contribution plans.

The adjustable pension plan was conceived by Richard Hudson, principal consulting actuary at Cheiron Inc., New York. Its key difference from a traditional DB plan is that the benefit received each year is adjusted from an original multiplier based on the previous year's investment performance.

The plan design shares the investment risk between employees and employers while providing more retirement income security than a typical defined contribution plan.

Earlier this month, Consumers Union, Yonkers, N.Y., reached a collective bargaining agreement with the Newspaper Guild of New York to create an adjustable pension plan that will replace the standard DB plan for guild members. The existing plan had about $42 million in assets as of Dec. 31, 2011, according to the company's most recent Form 5500 filing. That plan will be frozen on May 31, and contributions to the adjustable plan will start June 1.

Consumers Union, publisher of Consumer Reports, is the second single-employer plan to switch to the adjustable plan. Last November, The New York Times became the first with its $280 million plan for employees who belong to the newspaper guild.

The very first adopter of the adjustable plan was the Greater Boston Hospitality Employers Local 26 Trust Funds. The multiemployer plan adopted the new design on Jan. 1, 2012, moving from a 401(k) to a pension plan to provide more retirement security, according to a document on the union's website. Under its plan, participants will receive either a guaranteed floor benefit or the adjustable benefit tied to investment performance, whichever is greater. (The 401(k) plan, which had $35 million as of June 30 according to its latest 5500 filing, is still open, but there no longer is an employer contribution.)

6% contribution

Under the Consumers Union plan, the employer will contribute a fixed 6% of salaries plus $100,000 each year. The New York Times will contribute about $9.5 million to its plan this year and a similar amount after that based on a formula.

“It will vastly reduce risk and volatility for the company and still provide a lifetime payment and PBGC insurance,” said William O'Meara, president of The Newspaper Guild of New York. “We're hoping that this becomes a national model for others to adopt. There is some upside potential and very little downside for employees” compared with participant risks in a defined contribution plan.

However, both plans still need approval from the Internal Revenue Service - by July 31, 2014, for The New York Times and March 15, 2015, for Consumers Union. If the plans do not receive approval by those dates, the APP will revert to a new DC plan.

An official at the Pension Benefit Guaranty Corp., who declined to be named, said the new adjustable plan sounds like a “great idea.” But the plan won't be covered by the agency unless the IRS says it is a tax-qualified plan. If that designation is granted, it will be treated like any other DB plan, the official said.

An IRS spokesman did not respond to requests for interviews. However, Mr. Hudson said he has met with IRS and Treasury Department officials and did not think it would be a problem receiving approval.

Sources said the plan design makes sense for employers with union pension plans because they have collective bargaining rights, which can often prevent, or slow, a move to DC plans.

Interest from Maine

Still, the state of Maine is considering the APP for employees and teachers participating in the $11.5 billion Maine Public Employees' Retirement System, Augusta. Cheiron is Maine's actuary.

Maine employees are exempt from Social Security and the Legislature created a task force two years ago to design a supplemental plan for new employees who would also receive Social Security for the first time. The result was a hybrid within a hybrid — half adjustable pension plan and half DC plan.

“Maine would become the first state to enter Social Security from a non-Social Security position,” said Sandy Matheson, executive director of Maine PERS.

The task force has drafted legislation to create the new plan and is awaiting a bill sponsor. Ms. Matheson said it is unlikely the proposal will be picked up during the current legislative session.

“The Legislature had very specific criteria for us to work with,” specifically long-term cost exposure of 2% of salaries, and the task force “agreed on the principles we wanted to see in the plan,” Ms. Matheson said. One percent each would go to the DB and DC components, with a 6.2% contribution to Social Security, equaling a total 8.2% employer contribution.

The state contributes 3.67% of payroll to the state employees and teachers plan in addition to unfunded actuarially liability cost, which equals 11.59% and is expected to increase to 13.43% for the next two years.

The task force wanted to provide new hires with benefits as close as possible to the traditional pension plan, Ms. Matheson said.

Cheiron's Mr. Hudson said a plan needs to immunize retiree liabilities, instead of "letting it ride" on a 60% equity/40% fixed-income portfolio that does not take into account how much of a plan's liabilities are tied up with retirees. There should only be risk in the active group, he added.

Risk transfer

When moving to a DC plan from a DB plan, all the risk is transferred to the employee, Mr. Hudson said.

"Plans increase the risk first and then pass it on to employees. So we said we can do that without increasing the risk," Mr. Hudson said. "If you can't handle the risk you have, how would (participants) be able to take on more risk on their own?"

Under the APP there is a cut in benefits, Mr. Hudson acknowledged, but much less than with a move to a DC plan — and there is guaranteed retirement income.

"It might be a lower benefit than the traditional defined benefit plan, but at least it's secure," said the person from the PBGC. The official added that the adjustable plan is more cost controlled than a traditional DB plan and not as dependent on big contributions.

What differentiates the adjustable plan from a cash balance plan is that the cash balance plan benefit is determined by a benchmark such as 10-year Treasuries; the adjustable plan's benefit depends on actual investment performance of the plan.

Bruce Cadenhead, chief actuary for U.S. retirement at Mercer LLC in New York, said the adjustable pension plan is similar to the variably annuity plan design that has been around for decades but differs in that the employer still bears investment risk.

"I think it's something we're beginning to see more discussion about," Mr. Cadenhead said. "I think (this type of plan) is promising because one of the biggest risks is more people becoming retirement ready that will outlive their money, and this design addresses all those concerns."

The APP has an emphasis on low volatility and uses a lower discount rate. Mr. Hudson said the goal is get down to around a 6% return target with a standard deviation of about 5.5% to 6%.

'Essential principles'

The important part of the APP is that it includes all the "essential principles" for a new pension plan design such as employer contributions, pooled assets that are professionally invested and lifetime income, said Karen Ferguson, director of the Pension Rights Center, Washington. The PRC is in favor of any DB plan designs that address those principles, she added.

"It significantly reduces the risk to employers and employees," Ms. Ferguson said. "If the plan doesn't do well, then (participants) won't get a better benefit."

The adjustable plan idea probably is most appealing to unions because it helps to have bargaining power for better pension plans, Ms. Ferguson said. And unlike other alternative plan designs, the adjustable pension plan does not need legislative approval.

"It's so logical and makes so much sense," Mr. Hudson said. "When people ask why isn't everyone doing this, I just say, "I don't know.'

Pension reform passes Kentucky legislature

By Mike Wynn, The Courier-Journal , March 26, 2013

With only hours remaining in the 2013 legislative session Tuesday night, Kentucky lawmakers passed a landmark pension reform deal to shore up the state's struggling retirement system and help stave off a looming financial crisis.

The package involved two bills to overhaul and fund Kentucky Retirement Systems, the pension program for state and local workers that faces $18 billion in unfunded liabilities and administers one of the worst-funded plans in the nation.

Both measures — Senate Bill 2 and House Bill 440 — passed the House and Senate with bipartisan support following weeks of negotiations between legislative leaders and Gov. Steve Beshear.

Supporters hailed the move as a critical turning point in what many viewed as the most pressing issue facing the state legislature, and the bills now go to Beshear for his signature.

"This is indeed one of the greatest policy achievements of this body and this General Assembly in recent memory," said Senate Majority Leader Damon Thayer, a Georgetown Republican and sponsor of SB 2.

Beshear, who brokered the compromise, also praised it as a bipartisan solution to address Kentucky's looming pension liabilities without gutting funds for education.

But critics painted the deal as a slam to workers and a "smoke and mirror" diversion that will jeopardize retirement security while failing to provide any true pension reform.

Rep. Jim Wayne, a Louisville Democrat and opponent of the measures, said he felt like he was at a used car lot being sold a "clunker" and charged that workers and retirees were left out of process.

"What we end up with is a plan that is not stable," he said. "It's subject to the whims of the stock market."

The compromise in SB 2 is similar to provisions proposed by a legislative task force on pensions last year. It requires that cost-of-living adjustments be prefunded and will create a new hybrid retirement system for future hires that guarantees a 4 percent return while basing additional benefits on investment performance.

It also mandates full funding of the pension system by fiscal year 2015 and will place new lawmakers and judges into a hybrid plan rather than the traditional pension system.

HB 440 — the funding bill — involves eliminating an income tax credit and offering a car trade-in credit as part of a package to generate nearly $96 million in new revenue for pensions by 2015, and $99.9 million a year later.

Specifically, it will reduce a $20 personal income tax credit to $10, providing about $32.5 million for the state. Lawmakers sought to offset that change with a trade-in credit for new cars that will reduce the road fund by $34 million and create what proponents view as a net benefit for taxpayers.

The measure also calls for about a dozen smaller technology and tax compliance reforms to collect an additional $33.2 million that is already owed, and lawmakers anticipate $30 million in added revenue from federal tax law changes under the federal 'fiscal cliff' deal.

Stumbo, D-Prestonsburg, said House Democrats wanted to fund the system, preserve cost-of-living adjustments and protect the state's traditional defined-benefit plan rather than create a hybrid pension plan for new hires.

"We got two out of three, so I think our membership felt pretty good about it," he said. "And we protect every person that is currently employed."

Still, he argued on the House floor that the 4 percent guarantee in the hybrid plan was a "dag gone good deal."

In total, the state faces $33 billion in unfunded pension liabilities when counting Kentucky Retirement Systems and other pension plans for teachers, lawmakers and judges. But the teachers' system is not part of the reforms.

Looming pension liabilities prompted Moody's Investor Service to downgrade Kentucky's bond rating a year ago and Standard and Poor's Rating Service has revised the state's outlook from stable to negative — all part of the impetus for this year's overhaul.

The proposal does not designate the new revenue specifically for pension payments, as House Democrats and public unions had wanted. But it will provide a reoccurring source of new money in the state general fund, Stumbo said.

Lawmakers said that bond rating agencies prefer that approach over a designated funding stream, and Senate Republicans have long argued that legislature should negotiate a funding deal during budget writing next year.

Beshear said he was not concerned that the legislature will continue to shirk pension payment going forward and pledged that he will propose a budget next year with full funding.

The governor also rebuffed questions on whether the funding plan would essentially create a tax increase on everyone who does not trade in a car.

"We are hoping that everyone will buy a new car," he said. "We are an automotive state."

The policy reforms in Senate Bill 2 are expected to save about $10 billion over the next two decades. Thayer said those changes will save the retirement system from a financial crisis that could cost about $1 billion annually only four years from now.

"This is a big deal that saves the pension system and saves retirement for current employees and existing retirees," he said.

But unions and public worker groups were critical of the plan, and opponents said it will pass too much risk to state employees, jeopardizing their retirement security.

Jim Carroll, co-founder of Kentucky Government Retirees, cited deep concern that the compromise "fails to earmark revenue to specifically ensure the future stability of the pension fund. For the sake of all taxpayers, it is critical that future legislatures honor this financial commitment so that such a fiscal crisis is not repeated."

Steve Barger, coordinator for the Kentucky Public Pension Coalition, a group of 20 unions and advocacy groups, said members are also worried that the deal was cobbled together too hastily in the last week of the session.

"We didn't have an opportunity to fully review the language or the funding," he said. "I don't know that a lot of legislators had an opportunity."

The House voted 70-28 for SB 2 and 82 to 17 for HB 440. The Senate voted 32 to 6 on SB 2 and 35 to 3 for HB 440.

Beshear had warned again Tuesday morning that he would call a special session — at a cost of $60,000 per day — if the legislature failed to reach an accord before final adjournment.

Thayer said different proposals on funding and the hybrid plan were the main sticking points between the Democratic-led House and GOP-controlled Senate. But added later that he was confident the compromise would resolve the state's pension crisis.

"It's going to take a while," he said. "We didn't get in the problem overnight and we are not going to get out of it overnight."

Additional Facts

THE PENSION COMPROMISE

• Requires cost-of-living adjustments to be prefunded.
• Creates a new hybrid retirement system for future hires that guarantees a 4 percent return while basing additional benefits on investment performance.
• Places new lawmakers and judges into a new hybrid plan rather than the traditional pension system.
• Reduces a $20 personal income tax credit to $10, which would generate about $32.5 million in new revenue by fiscal year 2015.
• Creates a trade-in credit for new cars.
• Calls for about a dozen smaller technology and tax compliance reforms to collect an additional $33.2 million
• Anticipate $30 million in added revenue from federal tax law changes.

Pension fixes attract praise and criticism

TOM LOTSHAW/The Daily Inter Lake | Posted: Friday, May 3, 2013 9:00 pm

Montana lawmakers are getting praise but also some criticism and even threats of a legal challenge for their approach to fix hundreds of millions of dollars of unfunded promises in the state's two biggest public pension systems.

Plugging shortfalls in the Teachers Retirement System and the Public Employees Retirement System and making them actuarially sound as required by the Montana Constitution was a top priority for the 2013 session.

Two reform bills endorsed by Gov. Steve Bullock that promise to make both pensions sound almost overnight are on his desk awaiting his signature, albeit with a controversial amendment that caps cost-of-living adjustments for retirees.

House Bill 454 fills an estimated $1.8 billion funding shortfall in the Public Employees' Retirement System with coal tax money and 1 percent bigger contributions from employees and employers.

"To be actuarially sound, you have to be able to pay it in 30 years," said Roxanne Minnehan, director of the Montana Public Employees Retirement Administration.

The administration oversees the Public Employees Retirement System as well as several other unaffected pension programs in place for judges, sheriffs, police, highway patrol officers, firefighters and game wardens.

"We're going from infinity, where the actuary can't even calculate it, down to 15 years. That's a big jump. So it fixes the issue," Minnehan said of the Public Employees Retirement System.

Opposition has surfaced to a legislative amendment that reduces and caps the guaranteed annual benefit adjustment for retirees that was as high as 3 percent a year.

"This amendment reduces it to a ceiling of 1.5 percent and a floor of 0 percent, calculated annually based on how the pension fund is doing," Minnehan said.

That cap plays a big role in the fix.

But Minnehan expects the provision to be challenged in court. "The original bill didn't get us there immediately like this one does. It did it in like six years. I'm a little disappointed that has to be done on the backs of retirees," she said.

Bullock's office opposed the amendment and questioned its legality, Budget Director Dan Villa said. "We understand that both current employees and retirees are considering legal challenges to address the amendments and we support that action. It's important to keep in mind that this likely unconstitutional amendment doesn't change one important fact: By implementing the remainder of Governor Bullock's plan, Montana is the first state in the nation to fix our pension system without raising taxes," Villa said.

Villa added: "Failure to act now would pose an event greater risk to current and future retirees."

Under the proposed fix, employers can be tasked with gradually contributing up to an additional 1 percent if that becomes necessary to keep the fund's liabilities payable in less than 25 years.

The pension fix is supported by the Montana League of Cities and Towns, Executive Director Alec Hansen said. Roughly 3,100 of the 28,500 people paying into the Public Employees Retirement System work for cities in the league.

“This is a huge financial obligation and I think the legislature did a terrific job putting together a reasonable program that will produce the results needed,” Hansen said. “I think most people are fairly satisfied.”

The 1 percent increase in employer contributions is anticipated to cost the league’s member cities a total of $1.2 million a year in pension payments.

“It does not include a new permissive levy to let cities or counties levy any additional taxes. We didn’t ask for that or want that. Our cities all told me that they could fund this,” Hansen said. “They’ll have to move some money around, no question. But it won’t result in a property tax increase above and beyond the cap. And I don’t think there will be any reductions in services.”

The employer contribution increase will cost Kalispell’s general fund about $20,000 a year, City Manager Doug Russell estimated.

On the hook for 7.07 percent salary contributions before the increase, Kalispell paid $363,551 into the Public Employees Retirement System last fiscal year, according to budget records.

Brady Pelc, an employee in Kalispell’s parks department and the president of the local chapter of the American Federation of State, County and Municipal Employees, said the Legislature’s fix passes the burden onto employees and employers.

Kalispell employees paid 6.9 to 7.9 percent of their total compensation into the Public Employees Retirement System before the change — a share that now ratchets up another notch. Many people will just see more money coming out of their checks, Pelc predicted. “It is a very nice retirement system. Not a lot of employers can offer a defined benefit plan like that, so I feel lucky and fortunate to have that offered to me, but it definitely comes at a cost.”

HOUSE BILL 377 to reform the Teachers Retirement System also is on the governor’s desk.

“The bill is probably a good compromise,” David Senn, the system director, said. “There’s probably something in there for anybody to like or dislike.”

With 13,300 retirees drawing pension checks and 18,400 employees paying into the fund, the system had accrued unfunded liabilities totaling almost $900 million, Senn said.

“Bottom line, our teachers and administrators and public schools will be asked to pick up a significant portion of the increase,” Senn said.

Teachers’ pension contributions will increase from 7.15 to 8.15 percent of their pay.

School districts also must pay 1 percent more. And like new teachers hired after July, districts also could face gradual contribution increases totaling up to another 1 percent if needed to keep the pension fund sound.

New teachers also will have to work for at least 30 years and be 55 or older before they can retire and draw a pension. Existing law lets them retire after 25 years at any age.

“Retirees will see a reduction in cost-of-living adjustments,” Senn said. “They’re 1.5 percent now and will go down to .5 percent until the system is 90 percent funded. After that we can start to make increases, but it cannot result in the system going below 85 percent funded.”

Mike Thiel, a teacher at Flathead High School and president of the Kalispell Education Association, applauded the Legislature for coming up with a shared solution and fixing a system that needed fixed. “It was a problem that needed to be solved,” Thiel said. “Neither was perfect, but they both saved the idea of a pension and that’s pretty important for government employees and teachers.” Compared to the reduced cost-of-living adjustments, saving that pension system is the important thing, Thiel said.

“I’m friends with people retired out of both systems, and both groups are frustrated that retirees won’t get the guaranteed adjustment. But the message ought to be, ‘Let’s be patient.’ The [guaranteed annual benefit adjustment] is not the pension. The bottom line is we still have a defined benefit pension. We saved the pensions and the state of Montana should be proud of that. Name another state that did that.”

April 2013

Are public pension systems on the road to recovery?

Since 2008, public interest in the health of state and local pension systems has been consistently strong. The financial crisis caused systems’ funding levels to drop dramatically, requiring increased contributions from governments even while revenues were in short supply.

The news has been much better recently. The Dow Jones now stands at a record high, having more than doubled in value in four years. Nor have governments simply been waiting for the stock market to bail them out. According to the National Conference of State Legislatures, nearly every state passed some version of pension reform between 2009 and 2012.

But current struggles over pensions in Illinois and in California with the state’s CalSTRS system suggest that all may not be well. Many systems are still burdened with significant shortfalls, which put governments in the awkward position of effecting some combination of reducing funding for other priorities to support pensions; deferring payments to pension plans, likely leading to higher costs in the future; reducing pension benefit levels for current employees or even current retirees; or increasing contributions from current workers. Moreover, what it means for a pension system to be “well-funded” remains controversial, as new accounting standards set to take effect soon will cause some systems to appear worse off than at present.

So how to make sense of these mixed signals? Are public pension systems on the road to recovery?

Jason Richwine, a senior policy analyst in empirical studies at the Heritage Foundation, specializes in education policy and its intersection with public-sector compensation and labor issues. FULL BIO >>

Keith Brainard is research director for the National Association of State Retirement Administrators. FULL BIO >>

DAY 1 - OPENING REMARKS

Jason: Public pensions are in better shape than they were four to five years ago, but I see no

Keith: An abundance of evidence, the opinion of credible experts, and simple math confirm that signs that full funding—i.e., pension assets equaling the present value of pension liabilities—will be achieved in the near future. We are not on the road to "recovery" in any meaningful sense of the term.

Don't we just need to wait for the stock market to go up a little more? Or maybe tweak employee contributions and COLAs here and there? No. The fundamental problem is that public pension funds are not honest about the size of their liabilities.

Many readers of PSI are familiar with the accounting issue that I'm referring to. In the same way that $103 paid next year may be worth only $100 today, future pension liabilities must be discounted to reflect the time value of money. But discounted by how much? Public pension funds apply a discount rate equal to the expected rate of return on plan assets, which is usually in the range of 7 percent to 8 percent.

That choice of discount rate effectively ignores the cost of risk-taking by public pensions. Pension funds *might* achieve 8 percent average returns, but they *must* pay their promised pension benefits regardless. Thus, the present value of public pension liabilities is much greater than the "expected" cost published by the plans themselves. Additional liability comes from the guarantee that benefits will be paid even if a plan's risky investments do not generate the predicted returns.

Consider how irrational it is to ignore the price of risk. Riskier investments typically come with higher expected returns but also greater chances for a major loss. Under current accounting rules, only the expected return matters. So public pensions can appear better funded simply by taking on more risk!

Plan investments have at best a 50 percent chance of meeting their projected average returns over time, but there is a virtually 100 percent chance that promised benefits must be paid. This gap between mere expectation (of returns) and certainty (of benefits) comes at a cost that public pensions refuse to acknowledge.

Economists hoped that new accounting

public pensions are recovering. This recovery is evident especially when public pensions are viewed in their proper context, which is over the long-term.

Since 2009, after global investment markets had dropped more sharply than at any time since the Great Depression, nearly every state has made changes to restore or preserve the sustainability of its pension plans. These changes include higher employee contributions and lower benefits; in several states, benefits have been reduced even for employees who already are retired.

Such reforms to public pensions are nothing new: in a 2011 analysis, Standard & Poor's said, "state governments have a long-term track record of making adjustments and improving funding ratios." This time is no different.

Because public pensions are inextricably tied to the U.S. and global economies, predicting their demise requires one to hold a similarly bleak economic outlook. Fortunately, state government revenues, which help fund public pension plans, have grown for 12 consecutive quarters following the Great Recession.

Likewise, global investment markets have recovered, exemplified by US equity markets, which have more than doubled since 2009. Even as public pensions have distributed billions in benefits to millions of retired public employees and their survivors, their assets have grown by more than 40 percent. At the end of 2012, the combined value of public pension funds exceeded $3 trillion.

Some pension plans are in trouble, particularly those whose employers failed to appropriately fund them, and those who approved benefits without ensuring a way to pay for them. But these are the exception, not the rule. The Center for Retirement Research at Boston College in May 2012 predicted continued improvement in public pension funding levels. This prediction was made under the Center's "most likely scenario" for the stock market, which has only increased in value since the projection was made.

Meanwhile, public pension obligations—the amount the plans owe—are growing more slowly.

guidelines from the Governmental Accounting Standards Board would lead public pensions to reveal the true size of their liabilities. But while the new "blended" discount rate will increase published liabilities, it still falls far short of reflecting reality.

That reality is that public pensions are underfunded not by the $800 billion or so claimed by the funds themselves, but something in the area of $3 trillion to $4 trillion, depending on the risk-adjusted discount rate used. Public pensions cannot be on any road to recovery while maintaining unfunded liabilities of this size.

This is due to several factors, including the many benefit reductions made around the country; to a declining number of state and local government employees; and to the low rate of growth in public employee salaries. As a result, public pension assets are growing faster than their obligations. When this happens, the road to recovery is more than an opinion, it's a mathematical fact.

DAY 2 - REBUTTALS

Jason: Keith Brainard and I agree that public pensions are in better condition today than they were four to five years ago. Our major point of disagreement seems to be whether pensions can come anywhere close to fully-funded status without fundamental reforms.

As I noted in my opening statement, public pension administrators calculate the present value of liabilities based on the assumption that their investments will definitely achieve the target rate of return. This means that a plan can be "fully funded" in the eyes of pension administrators even when there is a strong possibility that assets will be insufficient to cover liabilities.

True "full funding" means both that pension recipients will get the benefits they are promised *and* that taxpayers know they are not on the hook for any additional money. To obtain this status, pensions must have enough assets to cover liabilities calculated using a lower, risk-adjusted discount rate. Despite a stock market boom and benefit adjustments, virtually no public pension plan comes close to true full-funding status.

NASRA and other pension advocates often argue that risk-adjusting liabilities is not appropriate for the public sector. Risk adjustment is needed in the unpredictable world of corporate finance, as this argument goes, but governments are perpetual entities that don't have to worry about long-term risk.

Keith: As evidence for his opinion that public pensions are not on the road to recovery, Jason says he sees no signs they will achieve "full funding" anytime soon. This is beside the point: as long as a state, city, or other public sector employer continues to operate, there is no compelling reason for its pension plan to be fully funded at any particular time. Attaining "fully funded" status is an appropriate long-term policy objective; it also is ephemeral and its value is debatable. Many public pension plans have been less than fully funded for decades without presenting a problem to their employers, taxpayers, or plan participants.

Jason then argues that public pensions can't be on the road to recovery because they "are not honest about the size of their liabilities." He believes financial theory—not actual or projected experience—should determine public pension funding levels. A central belief supporting this theory is that public pension benefits are guaranteed. Yet this often is not true: benefits have been reduced and employee contributions have been increased in many states.

According to this theory, pension funding levels rise and fall with interest rates. The Governmental Accounting Standards Board (GASB) recently considered, discussed, and rejected this approach, and for good reasons. The GASB retained standards that permit public pensions, as long as they are projected to have assets, to measure their liabilities on the basis of their long-term expected investment return. This

That is a fallacy. Investments do not become less risky the longer they are held, so governments hold no special investing advantage simply because they are long-lived. Risk has cost in the public sector just as it does in the private sector.

In his opening statement, Keith downplayed the risk: "Because public pensions are inextricably tied to the U.S. and global economies, predicting their demise requires one to hold a similarly bleak economic outlook." But this is a major reason why risk *does* come at such a price. Pension shortfalls tend to occur during recessions—exactly when taxpayers have the least money available to bail them out. Private investors understand this, which is why no one would offer to insure pension funds against low returns without charging a hefty risk premium.

Accounting standards for public pensions in other industrialized countries require the use of a risk-adjusted discount rate similar to what economists advocate for the U.S. system. The International Public Sector Accounting Standards Board, for example, recommends using bond yields (not expected stock returns) to discount pension liabilities.

The U.S. public pension system stands largely alone in believing that the price of risk is zero. If public plans in the U.S. were to follow the accounting principles that everyone else does, taxpayers would understand that no pension "recovery" is forthcoming without major reforms.

method is intended to promote stability and predictability of required contribution rates, benefitting public sector employers and taxpayers.

Pension fund managers must make asset allocation decisions based not on financial theory, but to maximize investment returns within an appropriate level of risk. Also, policymakers need to know how much to contribute to the plan, not to comply with a theory, but to pay the plan's future obligations while keeping contribution rates reasonably stable and predictable. These are real-life decisions with real-life consequences; a theory is not helpful.

Measuring pension liabilities based on current interest rates, as Jason proposes, actually reveals more about the state of the bond market than the condition of a pension plan. This method is particularly fallacious when rates are artificially low, as they are now. Indeed, since 2009, as interest rates have dropped sharply, Jason's method would have resulted in a steep decline in pension funding levels, even as the stock market has doubled. This is what corporate pension plans have experienced: growing unfunded liabilities as equity markets improve.

Ironically, if interest rates were to rise to seven or eight percent, using Jason's theory, unfunded pension liabilities would disappear and pension plans would be fully funded! Under that scenario, would Jason still support this method for calculating pension funding levels?

DAY 3 - Question from Gus, a reader in Kenosha, WI

Let's get clearer on the meaning of "recovery"—I think that may be behind this controversy over "full funding." One way to think about this is in terms of what the Pew Center on the States calls the "squeeze" effect, which occurs when growth in pension costs outpaces growth in revenues, leaving less room in government budgets for basic services. Recovered pension system=no more "squeeze" effect, not now, nor in the future.

Keith-are we there yet? Are you confident that the reforms enacted since 2008 will be enough, on a permanent basis, to make pensions a stable and predictable expense for governments? If so, what is the source of your confidence? Jason-your proposals seem to point in the direction of even greater contributions on the part of governments, which would exacerbate the squeeze problem in a way that I'm not sure the public is on board for. In other words, isn't full funding something like a balanced budget for the federal government? Policy experts may debate it all they want, but actually to achieve it would likely entail major sacrifices on the part of the public.

Jason: Gus asks a good question: Am I arguing that annual pension contributions need

Keith: For an employer that continues to operate and to hire new employees, funding a to go up dramatically, and isn't that politically unrealistic?

Let me answer in a roundabout way. The proper *valuation* of pension liabilities is separate from the question of how to *pay for* those liabilities. The present value of a pension fund's liability is the same regardless of whether the fund is currently invested in stocks, bonds, private equity, or a checking account. So when economists argue for market valuation of pension liabilities, they are not automatically supporting any particular investment portfolio or contribution level.

Funding choices do affect how costs are distributed between current and future taxpayers. To understand that, think of pensions as having two types of costs. The first cost is whatever the government contributes to the fund today to help pay for accruing benefits. The second cost comes in the form of a contingent liability on future taxpayers: If today's contribution (the first cost) proves insufficient to cover the benefits that have accrued, future taxpayers must pay the difference.

If pensions invest sufficiently in what economists call a "matching portfolio," which would consist mostly of bonds, the contingent liability on future taxpayers would be practically zero. In that case, current taxpayers would bear the entire burden of providing pension benefits to current workers. Alternatively, pension funds could invest in risky assets, such as stocks. That would reduce current costs, but it would transfer some of the burden to future taxpayers who must cover any lower-than-expected returns. The greater the investment risk, the more pension costs are shifted from today's taxpayers to tomorrow's.

So part of the decision about how to pay for accruing pension liabilities depends on our view of intergenerational equity. If we feel that all pension benefits for this generation of workers should be paid for by this generation of taxpayers, then sizable investments in safe assets are needed. But if we're comfortable with shifting some of the burden to the next generation, then risky investments might be appropriate. Either way, however, the total cost of accruing pension benefits does not change. It's just a question of pension is less of a destination than a journey. Public employers—states, cities, school districts, etc.—are essentially perpetual entities. Unlike private sector employers, which can go out of business or be acquired, public employers reasonably can be expected to continue to provide services, to collect revenue, and to employ workers indefinitely. Meanwhile, the employer's pension plan continues to receive new entrants, collect contributions, manage assets, and distribute benefits.

Because the plan's actuarial experience—how long participants live, how fast their salaries grow, rate of investment return, etc.—is constantly evolving, the plan regularly reviews the actuarial assumptions used to determine the required cost of the plan, and makes adjustments as needed. And because new obligations accrue continuously, contributions flow in, and benefits are paid, the true value of reaching full funding at any given point is questionable. Rather than the plan's funding level, a more relevant factor in assessing the condition of a pension plan is whether or not funding its liabilities creates fiscal stress for the pension plan sponsor. Although a pension plan that is fully funded is preferable to one that is underfunded, a plan's funded status is simply a snapshot in a long-term financial and actuarial process, akin to a single frame of a movie that spans decades.

States and cities have been reforming their pension plans almost as long as their pensions have existed. What's different recently is the pace and breadth of reforms. Since 2009, nearly every state and many cities have made changes to their pension plans, a rate and span of change that is unprecedented. Some states have made reforms more than once and others are likely to do so.

The magnitude of the changes varies widely, generally based on the degree of the plan's funding challenge, but affected also by other considerations, such as the plan's legal protections. In some cases, the only change has been an increase in required employee contributions. In other cases, current plan participants, and even current retired members, have experienced benefit reductions.

A recent study by the Center for Retirement how those costs are distributed.

Now, to directly answer Gus's question, full funding of public pensions at their current generosity surely would involve a "squeeze" to some degree on other government activities. But larger pension contributions in safer assets would dramatically reduce the chances of what we might call a "cyclical squeeze." This occurs when a pension's funding health declines alongside the economy, and governments must squeeze the public through higher taxes and fewer government services at a time when money is most scarce. Far from being "beside the point," as Keith put it, this is the danger posed by a substantially underfunded pension system.

Research at Boston College assessed a sample of the pension reforms made in recent years. They found that "for most plans, the reforms fully offset or more than offset the impact of the financial crisis on the sponsors' costs." They also found that "for the sample as a whole, pension costs as a share of state-local budgets are projected to eventually fall below pre-crisis levels."

Public pensions are causing fiscal stress for some states and cities. Usually this is a result of the employer's failure to make required contributions, or approval of benefits without ensuring a way to pay for them, or both. If they have not already, states and cities so affected will need to make changes. But on a national basis, as a share of state and local spending, public pensions cost much less today than they did 20 years ago.

DAY 4 - CLOSING REMARKS

Jason: Our debate has focused on how to properly measure the cost of a public pension. My contention, backed by basic economics, is that relying on risky investments places a contingent liability cost on future taxpayers: If the stock returns don't pan out, then those taxpayers have to make up the difference. In dismissing this contingent cost as a mere "theory," Keith and other pension advocates essentially deny that guaranteeing returns on risky assets has a price.

This is difficult to square with common sense. If true, why don't investors offer insurance to public pensions for virtually no cost? And if a pension's risky investments are somehow guaranteed, why not release taxpayers from their legal obligation to cover any shortfalls? The answer to both questions is: "Because risk isn't really costless."

Let's think about this more formally. In financial markets, investors can purchase the right to sell a security for a certain price at a later date. These "put options" can function as insurance against low returns. For example, a pension fund could buy a put option that gives it the legal right to later sell an investment at a price that reflects its expected annual rate of return of around 8 percent. Even if the investment performs worse than that, the pension fund is guaranteed to

Keith: Our nation faces a retirement crisis. As the Wall Street Journal editorial board said in 2010, "The biggest, but most underreported, financial story in America is the looming retirement disaster. Eighty million baby boomers are approaching retirement, and most have absolutely no idea what's going to hit them. For them the financial crisis isn't over. It's just about to begin."

The funny thing is that we are in this predicament despite knowing which retirement policies work and which ones don't. A wiser retirement policy should begin by viewing retirement security not as an experiment in wealth accumulation, but as a form of old-age income insurance.
There is a place for defined contribution plans in our nation's retirement policy (see *three-legged stool*), but if we have learned anything from a generation reliant on defined contribution plans as their primary retirement benefit, it is that on-your-own retirement planning and saving does not work very well.

Another policy that doesn't work well is the current model governing corporate pension plans, which ties pension valuations and required costs to current interest rates. Despite the best of intentions to protect pension benefits, this policy receive its expected funding.

Here's the catch: Put options are not free. In fact, the cost of a put option will be the same as the cost of simply using the lower, risk-adjusted discount rate that economists advocate. So despite the belief of some pension advocates that risk adjustment is a theory disconnected from reality, such accounting reflects actual practice in real-world financial markets.

Keith noted that the "theory" I'm espousing indicates that pension funding varies with interest rates. Of course it does. Interest rates determine the price of guaranteeing investments. It may be inconvenient that changeable interest rates make pension funding levels volatile, but that doesn't make it untrue. By contrast, Keith says that current accounting standards provide stability in contribution rates. They can do this only by ignoring what is actually happening in financial markets!

I'll conclude by answering the question Keith posed at the end of his rebuttal: If U.S. Treasuries (a virtually guaranteed investment) were today paying 8 percent per year, would I consider today's pension contributions sufficient to fully fund new benefits? The answer is yes, and there was a time when bonds did pay a yield that high. The trouble is that public pensions now pursue a risk premium over and above the Treasury rate. As I've tried to emphasize all week, risk comes at a price—a price that public pensions simply will not acknowledge.

has caused such uncertainty and volatility of required employer contributions, that most corporations that sponsored a pension benefit have closed theirs. Yet there are those who believe that the financial theory driving this methodology should be extended to pension plans for employees of state and local government.

Let's pursue retirement policies that work: mandatory participation, cost-sharing between employees and employers, pooling of assets, and required annuitization of benefits. These features define retirement plans for most employees of state and local government, and there is nothing inherent in those policies requiring them to be expensive or exceedingly generous.

A well-designed public retirement plan benefits all stakeholders, including employers, who must attract and retain qualified workers needed to perform essential public services; taxpayers, who share in the cost of these benefits and who rely on the services public workers provide; and employees, who seek competitive compensation and the opportunity to retire in dignity.

Some opponents of public pensions point to the unfunded pension liabilities of state and local governments as a reason to eliminate those retirement plans, even as they overlook our nation's estimated $6.6 trillion retirement savings shortfall.

Retirement security benefits everyone, and when others have a secure retirement, we all are better off. The answer to our nation's retirement crisis is not found in a policy driven by a financial theory, nor is it to dismantle some of the last remaining decent retirement benefits. The solution to our nation's retirement crisis is in public policies that encourage the creation and retention of retirement plans with features that work. We simply need the wisdom to recognize them and the political will to implement them.

Jason Richwine, a senior policy analyst in empirical studies at the Heritage Foundation, specializes in education policy and its intersection with public-sector compensation and labor issues. Richwine joined the Domestic Policy Studies department in January 2012. He previously was part of the think tank's Center for Data Analysis. Richwine has published dozens of op-eds in *The Wall Street Journal*, *The New York Times*, *The Washington Post*, *National Review*, *The Weekly Standard*, *The Atlantic*, and *Huffington Post*. He

Keith Brainard is research director for the National Association of State Retirement Administrators. He creates and maintains the Public Fund Survey, an online compendium of public pension data sponsored jointly by NASRA and the National Council on Teacher Retirement. He has discussed public pension issues before Congress, state legislative committees, public pension boards of trustees, and on broadcast television and radio. Mr. Brainard previously served as manager of budget & planning for the Arizona State received his doctorate in public policy in 2009 from Harvard University. He holds bachelor's degrees in mathematics and political science from American University.

Retirement System. He has a master's degree from the University of Texas at Austin, LBJ School of Public Affairs. He is co-author of *The Governmental Plans Answer Book, nd Edition*.

Corruption and Public Pensions

by Ady Dewey

Hand, *n*, A singular instrument worn at the end of a human arm and commonly thrust into somebody's pocket. *The Devil's Dictionary*

When the seemingly deep-pocket world of public pensions is combined with human nature, it may be easy to understand how corruption might occur.

Or, as Al Lewis writes in *The Wall Street Journal*,

Once some folks get their hands on other people's money they suddenly think it's their own.

This is why nearly every state retirement plan has rules for bidding services and contracts, so they are provided in an environment that is open and competitive. And it is why plans have established gifts and ethics guidelines whether by policy, statute or code (see a 2007 compilation of public retirement system gifts and ethics policies by the National Association of State Retirement Administrators).

While the length and wording of such policies varies, most public retirement systems are based on the principle expressed in the succinct statement of the North Dakota Teachers Fund for Retirement:

Board members shall refrain from financial and business dealings that tend to reflect adversely on their impartiality or interfere with the proper performance of their duties.

The Michigan Office of Retirement Services has Rules of the Civil Service Commission regarding ethical standards, and guidelines to comply with those rules, as presumably does the City of Detroit pension fund.

But that did not stop the hands of a few public officials from filling their own pockets as Detroit Free Press reported:

"Public officials entrusted with billions of dollars in employees' pension money cannot take bribes and kickbacks to influence their investment decisions," U.S. Attorney Barbara McQuade said of the latest charges Wednesday.

The government's latest charges…revealed lavish travel by trustees and staff, questionable dealings by secretive middlemen and repeated incidents in which the funds' investment adviser failed to detect potential problems in the backgrounds of several businessmen pushing deals.

While the trial in Detroit is just beginning, indictments were announced in California for former CalPERS chief executive officer Fred Buenrostro and a former Board member, Alfred Villalobos. Buenrostro was indicted on five counts including fraud, making false statements to the U.S. government and obstruction of justice; and Villalobos was indicted on three counts including fraud, mail and wire fraud, and making false statements.

As the current CalPERS CEO announced via Twitter:

Ms. Stausboll went on to say in a statement: “The trust of our members, employers and stakeholders, and CalPERS own core values, are the heart of our organization and we will not let the selfish and illegal actions of a few individuals define our organization, our members or our staff.”

The public pension community is made up of more than 3,000 public pension funds holding more than $3 trillion in trust for 15 million working and 8 million retired workers. In the main, the investment performance of these funds compares closely to those of other institutional investors, such as corporate pension funds and endowments. The cost of investing public pension fund assets is less than one-half of one percent of assets per year.

Public pension funds live in a fishbowl, complying with open records and open meetings requirements, publishing detailed financial reports, etc. Nearly all public retirement systems are overseen by a board of trustees who are fiduciaries—charged to operate solely in the interest of plan participants.

The combination of investment performance, modest costs, transparency, and oversight illustrates a community that, for its size and breadth, experiences a remarkably low level of graft and corruption.

This is why the indictments in Detroit and California are so newsworthy—because they are the exception.

The transgressions of a few do not define the whole, whether within one pension fund or across the industry. And it is critical if a random hand is held out that it is quickly slapped.

PUBLIC-SECTOR PENSION PLANS

Major Challenges & Common-Sense Solutions

BY KIM NICHOLL

Ensuring that state and local pension plan funding will be adequate to support promised benefits is a critical task for policymakers. Assessing funding adequacy starts with having a reliable measure of the plan's cost, in both the short and long term. For a defined benefit pension plan, an actuarial funding policy determines the ultimate cost of the plan and how much of that cost should be contributed in the current year. Then, if actual contributions are less than the actuarially determined cost, at the most basic level two options are available: 1) reduce the cost of pensions by restructuring benefits, and/or 2) increase the amount that public employers (i.e., taxpayers) and/or employees contribute to the plan. In some jurisdictions, modest changes in benefits or contributions will be sufficient to fill the gap, but in others, often where unfunded liabilities are large, more substantial revisions will be required.

ACHIEVING BALANCE

Stakeholders have different priorities and will naturally advocate reforms that reflect those priorities. Taxpayer organizations tend to focus more on paring back pension benefits in order to reduce pension costs, while employee groups, concerned about their ability to achieve a secure retirement, often prioritize increased plan funding.

> Assessing funding adequacy starts with having a reliable measure of the plan's cost, in both the short and long term.

A balanced approach is more likely to achieve success than an either-or proposition. Each group of public pension stakeholders has legitimate objectives. Taxpayer concerns about the affordability of pension benefits and employee concerns about having sufficient retirement income are both valid. And both groups should share an interest in seeing that sound pension funding principles are being followed. Beyond these considerations, public employers have their own workforce management objectives — they want to ensure that the pension benefit, as part of an overall compensation package, supports their efforts to hire and retain talented employees. If they are to address the needs of all parties in the long term, reform efforts must take all these priorities into consideration.

The best way to achieve balance among stakeholder priorities is to align the policies governing pension funding and pension benefits with broad public policy goals, rather than narrow interests. These goals might include transparency, budgetary predictability, benefit affordability, retirement security, intergenerational equity, and the provision of high-quality public services. While it might seem impossible to meet all these objectives simultaneously, policymakers can rely on some common-sense principles to maximize their chances of achieving balance among competing aims.

A COMMON-SENSE APPROACH

Before delving into the details of pension funding policy, it is important to clarify that state and local pensions are pre-funded, as opposed to pay-as-you-go retirement systems like Social Security. In pay-as-you-go systems, contributions from current employees are used to pay benefits for current retirees. In pre-funded systems, the employer and employee make contributions into a pension trust each year, over the course of an employee's working life. That money is invested and earnings on these funds are re-invested. By the time the employee reaches retirement, the accumulated assets in the trust are available to pay benefits. The objective, of course, is to accumulate sufficient assets to pay the benefits over the remainder of the employee's life, and any beneficiary's life as well.

To meet this objective, a pension plan should receive contributions in accordance with an actuarially based funding policy. The funding policy determines exactly how much the employer and employee should contribute each year to ensure that the benefits being earned will be securely funded in a systematic fashion.

A comprehensive and actuarially well-designed funding policy supports three key policy goals: predictable costs for employers, secure benefit payments for members, and intergenerational equity across different groups of taxpayers.

Predictable Costs for Employers. If pension contributions fluctuate wildly from one year to the next, the result is budget chaos. That creates problems for all stakeholders. Thus, a funding policy should be purposely designed to develop costs that are expected to bear a reasonable relationship to payroll and to manage and control contribution volatility. A comprehensive funding policy has several moving parts, including an actuarial cost method, asset-smoothing techniques, and the manner in which any unfunded liabilities are amortized. A plan's specific choices for each of these policy components will have a bearing on whether employer pension contributions will be more predictable or more volatile. In addition, contributions must be based on actuarial assumptions, both demographic and economic, that reflect the best possible estimates of future experience.

The actuarial cost method refers to the manner in which the total present value of all future benefits for current active participants is allocated to each year of service. Asset-smoothing techniques are a tool used to manage the effect of investment volatility on contributions and to provide a more consistent measure of plan funding over time. Financial markets have considerable short-term volatility, but pension plans have long investment and benefit horizons. Asset-smoothing methods are used to reduce the effect of that short-term market volatility on contributions, while still tracking the changes in the market value of plan assets. They do this by recognizing the effects of investment gains and losses over a period of years, instead of immediately when they occur. Amortization of unfunded liabilities refers to the manner in which the current and future unfunded liabilities are systematically funded, or "paid off," over time.

While a detailed review of these complex issues is beyond the scope of this article, it is important to note the following general rules.[1] The "entry age normal" actuarial cost method tends to recognize actuarial liabilities sooner and tends to result in a more stable normal cost pattern over time, as compared with other methods (such as the "projected unit credit" method). Determining the ideal asset-smoothing policy involves a balance between controlling market volatility (by using longer smoothing periods) and making sure the smoothed asset value maintains a reasonable relationship to the actual market value. Amortizing unfunded liabilities involves balancing the two goals of ensuring fairness across generations of taxpayers and controlling contribution volatility for plan sponsors. Amortizing unfunded liabilities over longer periods will lead to less volatility in contributions, but excessively long periods may inappropriately shift costs to future generations. Plan sponsors must find a balance between controlling contribution volatility and ensuring that costs are not unfairly shifted to future generations of taxpayers.

Secure Benefit Payments for Members. The plan exists to pay benefits. For that reason, funding policies are designed to accumulate assets over time that will provide for all the benefits that have been and will be earned by plan participants. An actuarially determined funding policy generally supports this goal.

In some instances, employers' annual contribution rates are fixed by statute or otherwise not determined by strict adherence to a funding policy. Fixed contributions have the benefit of being very predictable, but they can pose risks by falling short of the actuarially determined needs of the pension plan, increasing unfunded liabilities. This is especially true when the plan has a limited ability to adjust benefits. Even in cases where the contribution rate, as originally established, was actuarially determined, changes in the plan or plan experience (e.g., benefit improvements, mortality improvements, and/or asset losses) can cause the fixed contribution rate to become insufficient for the plan to achieve its goal of paying all benefits when due. The result could be a rapid, unexpected escalation in actuarially required contributions, thereby adding to the employer's fiscal commitments.

Intergenerational Equity across Groups of Taxpayers. The goal of fairly sharing plan costs across generations of taxpayers is achieved by adopting a funding policy that ensures that the cost of pension benefits is reasonably allocated to the years of service worked by employees. A funding policy can help ensure that the cost of benefit improvements is recognized and paid for during the working careers of those who will receive them, without unfairly burdening the current taxpayers for events beyond their control.

The best way to achieve balance among stakeholder priorities is to align the policies governing pension funding and pension benefits with broad public policy goals, rather than narrow interests.

As noted previously, the objective of intergenerational equity provides a "check" to ensure that the goal of predictable contributions does not override all other concerns. Longer asset-smoothing and amortization periods help reduce contribution volatility, but by doing so, current taxpayers may be deferring costs to future generations of taxpayers. A balanced funding policy will find a "sweet spot" between these two important policy goals.

Once the plan sponsor has established the elements of a comprehensive funding policy and put it into effect, stakeholders should be able to understand the cost of pension benefits and develop a realistic plan for paying those costs over time. In many cases, stakeholders will be reassured about the path they have been following to meet future commitments. But sometimes, pension trustees, employers, and/or policymakers may discover that the commitments they have made in the past are not enough, and the plan will require greater contributions. Still others may find that their commitments are no longer affordable when considered in the context of the overall state or local budget and that benefits need to be reevaluated. In any of these scenarios, officials may also conclude that having a comprehensive statement of their funding policy in a single document is advantageous. A well-conceived funding policy can do more than ensure a well-funded plan — it can enlighten benefit policy.

COST — AND OTHER — CONSIDERATIONS

In the current environment, state and local governments' reexamination of their pension programs is being driven primarily by cost considerations. But there are other good reasons to review pension benefit policy periodically. These include assessing how economic risks are shared between employers and employees, reviewing the extent to which benefits provide an adequate retirement income, and ensuring that the plan is still meeting the workforce management goals of the employer, including employee attraction, retention, and retirement patterns.

State and local officials nationwide are focused overwhelmingly on the question of whether existing pension plans are affordable or sustainable, given new fiscal realities. There are many ways to achieve the goal of reducing pension costs, but some changes have a greater impact than others. Shorthand images or metaphors can help when ranking or

prioritizing changes according to their financial impact. For example, changes with the largest impact on cost can be thought of as "boulders." These might include eliminating cost of living adjustments or changing the basic design of benefits. Changes with large but less significant effects are "rocks." This category could include reforms such as modifying cost of living adjustments, increasing retirement ages, and changing eligibility rules or benefit formulas for current and future employees. Modest-impact changes can be thought of as "pebbles," and those with the smallest effects, "sand." Increasing the final average salary period use for calculating benefits from three or five years to five or seven years would fall into this category, as would reductions to disability and death benefits. Stakeholders can use this imagery to help them stay focused on changes that will make a real difference, and avoid being unduly distracted by modifications that might not ultimately address the core question of affordability.

DISTRIBUTION OF RISK

The type of retirement plan offered — a traditional defined benefit pension plan, a defined contribution savings plan, or a hybrid plan, which combines elements of DB and DC plans — has great bearing on how risks are distributed. Indeed, recent economic events have reminded employers that investment risk and the resulting contribution volatility risk have significant economic consequences.

DB and DC plans differ in how they allocate risks, including investment risk, inflation risk, contribution risk, and longevity risk. Under a DB plan, the employer bears the bulk of these risks. For example, if life expectancy increases, employer contributions will need to increase as well to cover the benefit payments for longer periods.[2] Under a DC plan, the employee bears these risks while the employer may be exposed to other risks, particularly workforce management. If investment earnings fall short of expectations, employees will need to save more, delay their retirement, and/or modify their standard of living during retirement.

Hybrid plans are designed to share risks between employers and employees by incorporating aspects of capital-accumulation (DC) and income-replacement (DB) plans. In the public sector, hybrid plans are typically structured as combination plans in which employees earn a portion of their retirement benefit in a DB plan and also participate in a DC plan. Generally, the employer bears the risks for the DB portion of a hybrid plan and the employee bears the risks for the DC portion.

Stakeholders may find it worthwhile to evaluate whether these risks are in their proper place and determine whether redistributing some of these risks is appropriate. This involves assessing which risks the plan or employers are in the best position to manage, and which ones employees can handle. Employees, with no opportunity to "pool" risk, may not be in the best position to bear the full brunt of investment, inflation, and — especially — longevity risks. There is also the matter of degree. For instance, employees might be able to bear some amount of contribution risk, but not all of it. A comprehensive benefit policy examines all aspects of risk and where it is most appropriately placed.

Benefit Adequacy. Even though the stark fiscal environment is pushing cost and risk considerations to the forefront, stakeholders need to keep sight of benefit adequacy. After all, the goal of a retirement plan is to allow employers to attract and retain talent at a reasonable cost to the taxpayer by providing some level of retirement security to employees as part of a total compensation package.

The "correct" benefit level should be based on objective analysis and subjective considerations. Benefit adequacy is typically assessed by calculating a "replacement ratio," dividing the amount of retirement income a career employee would receive from the plan and from other income sources by the employee's income just prior to retirement. Determining the "correct," or target, replacement ratio involves some subjective calls such as defining a career employee and determining the age at which the target should be set. In addition, plan sponsors need to consider how the target should be set for public safety employees, given their unique work environment and demands. Another important consideration in evaluating benefit adequacy is the availability and cost of health care in retirement.

A study conducted as part of Georgia State University's Center for Risk Management and Insurance Research's Retiree Income Replacement Project suggests that, as workers' pre-retirement income ranges upward from $20,000 to $90,000, they will need a 94 percent to 78 percent replacement ratio to maintain a similar lifestyle in their post-retirement years.[3] Social Security replaces 69 percent to 36 percent of pre-retirement compensation at these income levels. Therefore, the remainder needs to come from employer-sponsored pensions, employer-sponsored retirement savings plans, and personal savings. For those public-sector employees who aren't covered by Social Security (approximately 30 percent of the state and local government workforce),[4] the need for retirement income from an employer-sponsored plan and personal savings is greater, a fact that must be taken into consideration when setting benefit policy.

Plan sponsors must find a balance between controlling contribution volatility and ensuring that costs are not unfairly shifted to future generations of taxpayers.

Workforce Management Considerations. Employers offer benefit plans because such programs have been shown to aid in workforce management, supporting recruitment, retention, and the orderly retirement of employees. In general, employers can use plans that are designed to offer employees a more predictable benefit to accomplish workforce management goals, which include attracting experienced employees from the private sector, retaining talent, or facilitating orderly turnover through predictable retirements.

Nevertheless, the implications of plan type on workforce management are sometimes overlooked. Conversely, changes in the workforce or in HR management objectives might prompt a reexamination of plan design to ensure that it is consistent with overall HR strategy.

DB plan features can be used to encourage recruitment, retention, or retirement. Workforce management is more difficult with DC plans because account balances fluctuate with the financial markets, which can influence the timing of retirement beyond the control of the employer. In addition, the employer has little ability to encourage retirement through incentives if the existing DC plan balance will not support retirement income needs.

Careful planning and quality analysis are the keys to designing a successful benefit policy. Making changes in a kneejerk fashion in response to the immediate budget or the political environment might address the narrow affordability question, but is unlikely to result in a retirement program that meets the long-term needs of employers, employees, or taxpayers. Equal caution should be exercised to avoid making changes to benefits in a vacuum. Rigorous analysis of existing data and forecasting of future trends are both invaluable in helping stakeholders determine whether proposed changes will accomplish their objectives and avoid unintended consequences.

CONCLUSIONS

When comprehensive funding and benefit policies are in place, they work hand in hand to reassure all stakeholders that pension plans are meeting broad public policy objectives. The choice is not *either* to focus on funding *or* to focus on benefits, but rather to do both, in a considered, deliberative manner.

Stakeholders may not necessarily share the same objectives, or they may place different priorities on common objectives, but when it comes to pension reform, providing the opportunity for all voices to be heard enhances transparency and may improve the chances of stakeholder buy-in. The most successful and durable pension reform efforts are ones that strike a balance among recognizing employers' budget constraints, promoting responsible annual funding, and offering reasonable, secure benefits as part of a competitive overall compensation package. With comprehensive funding and benefit policies in place, pension plans will be well positioned to meet current challenges and to ensure that long-term goals are met as well.

Notes

1. For a detailed examination of these issues, see "Planning a Successful Pension Funding Policy," Segal *Public Sector Letter*, November 2011.
2. Employees in some DB plans can bear a portion of these risks, if their contributions are adjusted to reflect the impact of the risks on plan costs (i.e., contribution rates that change based upon the actuarial valuation).
3. These replacement ratios are noted on page ii of the 2008 GSU/Aon RETIRE Project Report, available at http://rmictr.gsu.edu/Papers/RR08-1.pdf.
4. *State and Local Government Retiree Benefits: Current Status of Benefit Structures, Protections, and Fiscal Outlook for Funding Future Costs*, U.S. Government Accountability Office, 2007.

KIM NICHOLL is a senior vice president and consulting actuary and the National Public Sector Retirement Practice leader of The Segal Company, based in the Chicago office. Nicholl is experienced with the design and interpretation of plan provisions for defined benefit and defined contribution retirement plans and on their relation to ERISA, IRS regulations, and new legislation, and her experience includes all aspects of employee benefit programs. She can be reached knicholl@segalco.com.

SOMEWHERE
Cash Balance Plans
IN THE MIDDLE

BY PAUL ZORN

The recent financial downturn and resulting economic decline have put substantial fiscal pressures on state and local governments. As a result, many states have made significant changes to their retirement plans. Most of the changes were made within the existing defined benefit framework. Generally, the changes involved: 1) increasing employee contributions; 2) lowering benefit formulas for newly hired employees; and 3) reducing postretirement cost-of-living adjustments. However, some states made more fundamental changes. While only a few established new defined contribution plans, several introduced plans that combine elements of DB and DC plans, including two states that recently established cash balance plans.

Cash balance plans are not new to state and local governments. The Texas Municipal Retirement System is a cash balance plan that has been operating since 1947, and the Texas County and District Retirement System is a cash balance plan that has been operating since 1967. In 2002, Nebraska established a cash balance plan to replace its DC plans for state and county employees. More recently, in 2012, Kansas and Louisiana also established cash balance plans. However, while cash balance plans are not new, their benefit design is fundamentally different from traditional DB plans. The goal of this article is to provide readers with a better understanding of how cash balance plans work and their key advantages and disadvantages.

> In considering the advantages and disadvantages of plan designs, the overall goals of both employers and employees need to be considered.

COMPARING PLAN DESIGNS

Although cash balance plans are legally considered to be defined benefit plans, they combine elements from both defined benefit and define contribution plan designs. To better understand how they work, it is helpful to compare them to DB and DC plans. The following discussion is summarized in Exhibit 1.

Defined Benefit Plans. DB plan benefits are typically determined using a formula based on an employee's years of service, final average salary, and a benefit multiplier representing the portion of final average salary earned each year. For example, given a 2 percent benefit multiplier, an employee retiring after 30 years of service with a final average salary of $50,000 would earn an annual benefit of $30,000 (i.e., 2 percent x 30 years x $50,000). Generally, the benefit is paid as a guaranteed lifetime annuity, and it often includes a postemployment COLA to protect retirees from inflation. In addition, most state and local DB plans also provide disability and survivor benefits that are based on service and salary. In a typical DB plan, the plan sponsor bears most of the risk.

Defined Contribution Plans. DC plans benefits are based on accumulated employer and employee contributions made to an employee's individual account, combined with actual investment earnings. Members usually have significant control over how their accounts are invested. The benefit depends largely on investment returns and is not guaranteed over an employee's lifetime. Generally, the benefit is paid as a lump sum, which can be rolled over into other retirement accounts. DC plans do not provide disability and survivor benefits, other than for the distribution of the employee's account balance. In a typical DC plan, the plan participant bears most of the risk.

Cash Balance Plans. Cash balance plans are similar to DC plans in that the benefit is based on an employee's account balance. Under cash balance plans, employees contribute a fixed percentage of pay and employers also provide contributions (referred to as "pay credits"). However, unlike DC plans, the account is a hypothetical "nominal" account that keeps track of the benefit accrual, but the related contributions and investment earnings are held and invested by the cash balance plan. Members typically have no say at all in how their nominal accounts are invested.

Interest is credited on an employee's nominal account at a fixed rate (or may be based on an index rate or other variable rate). For example, a cash balance plan could promise to credit interest to a member's account at an annual rate of 5 percent, regardless of the plan's actual investment returns. Consequently, the interest credited to an employee's cash balance account is generally less volatile than the interest earned by employees in DC plans.

Cash balance plans are similar to DB plans in that the plan sponsor bears most of the risk. Also, cash balance plans commonly provide retirees with the option of converting their account balances into lifetime annuities. Unlike most DB

Exhibit 1: Comparison of State and Local Retirement Plan Designs

	Defined Benefit Plan	Defined Contribution Plan	Cash Balance Plan
Basis of Benefit	Formula based on years of service, final average salary, and benefit multiplier	Account balance based on employer and employee contributions plus actual investment earnings	Nominal account balance based on employee contributions and employer pay credits plus credited interest
Benefit Distribution	Lifetime annuity with optional forms of payment. Some plans offer partial lump-sum distributions	Lump-sum payment, with ability to rollover to other qualified retirement plans	Lifetime annuity with optional forms of payment. Most plans also offer lump-sum distributions
Disability and Preretirement Death Benefits	Provided based on plan formula	Provided as a lump-sum distribution of the individual's account balance	Provided as an annuity or a lump-sum distribution based on the individual's account balance. In some cases, formula benefits provided through the existing DB plan
Postemployment COLA	Often the plan provides a COLA	Not offered	Some plans provide a COLA while others allow employees to purchase a COLA with an equivalent reduction in the annuity benefit

plans, cash balance plans usually allow lump-sum distributions. Similar to DC plans, cash balance plans do not usually provide disability or survivor benefits, other than for the distribution of the employee's account balance. For this reason, they may be less suitable for public safety employees whose jobs are more hazardous and, consequently, warrant more substantial disability and survivor benefits. However, some public-sector cash balance plans have been structured to provide disability and survivor benefits to plan members.

Another way in which cash balance plans are similar to DB plans is that both require actuarial valuations to determine the employer contributions needed to fund the promised benefits. Like DB plans, cash balance plans are subject to a variety of risks, including those related to investment returns, mortality, and inflation. While cash balance plans may help to mitigate some of these risks, they cannot eliminate them. The plan sponsor still bears the risk that terminations will be less than assumed, that salary increases will be more than assumed, and that investment returns will be less than assumed. If so, additional employer contributions will be required to make up the difference.

EXAMPLES OF CASH BALANCE PLANS

Since cash balance plans are conceptually different from DB plans, examples may help to illustrate how they work. Key elements of the following case studies are summarized in Exhibit 2.

The State of Nebraska. In 2002, the Nebraska Legislature established two cash balance plans, one for state employees and the other for county employees. The cash balance plans replaced DC plans, which were found to provide insufficient retirement benefits. The cash balance plans were mandatory for all full-time state and county employees hired on or after January 1, 2007. However, other employees were allowed to join the cash balance plans if they made an irrevocable election to do so.

State employees contribute 4.8 percent of pay, and county employees contribute 4.3 percent.[1] The state matches the contributions of state employees at 156 percent, and the counties match their employees' contributions at 150 percent. For both plans, interest is credited to the employees' accounts at a rate that is the greater of 5 percent or the applicable mid-term rate published by the Internal Revenue Service, plus 1.5 percent compounded annually. Employees are vested in their benefits after 3 years of service.

Cash balance plans are similar to DB plans in that the plan sponsor bears most of the risk.

In both plans, employees become eligible for their retirement benefits starting at age 55. The benefit is based on an employee's accumulated account balance, including employee and employer contributions plus credited interest. The normal retirement benefit is a single-life annuity with a 5-year certain period, although additional forms of payment are available, including full or partial lump-sum distributions. Disability benefits and in-service death benefits are based on an employees' account balance. The county plan also allows

Exhibit 2: Examples of Public Sector Cash Balance Plans

	Nebraska's Cash Balance Plans	Kansas' Cash Balance Plan	Louisiana's Cash Balance Plan
Year Established	2002	2012	2012
Covered Groups	State and county employees	Most new employees (except correctional officers) starting after January 1, 2015	After July 1, 2013, most new members of the Louisiana State Employees' Retirement System (other than hazardous duty positions). Also, post-secondary school members of the Teachers' Retirement System of Louisiana. (Subject to legal appeal)
Employee Contributions	State employees contribute 4.8 percent of pay; county employees contribute 4.3 percent of pay. Additional contributions from law enforcement employees	6.0 percent of pay	8.0 percent of pay
Employer Pay Credits	State matches employee contributions at 156 percent. Counties match employee contributions at 150 percent	Based on service (3 percent of pay for 1-4 years; 4 percent for 5-11 years; 5 percent for 12-23 years; 6 percent for 24+ years)	4.0 percent of pay
Credited Interest Rate	Greater of 5 percent or applicable mid-term rate published by the IRS plus 1.5 percent, compounded annually	5.25 percent guaranteed rate, with possibility of additional interest credits ranging from 0-4 percent based on investment returns	100 basis points below actuarial rate of return (i.e., rate based on smoothed value of plan assets), but not less than 0 percent
Vesting	3 years	5 years	5 years
Service Benefits	Single-life annuity with a 5-year certain period. Optional forms including full or partial lump-sum distribution with reduced annuity	Lifetime annuity. Optional forms including survivor benefits and a partial lump-sum distribution of up to 30 percent with reduced annuity	Lifetime annuity. Optional forms include partial lump-sum distributions with reduced annuity
Disability and In-Service Death Benefits	Annuity or lump-sum based on employee's account balance	Disability pay's 60 percent of current salary. In-service death benefits paid through life insurance and return of members contributions	Provided through the existing defined benefit plans

county employees to convert their account balance into a lifetime annuity with a postemployment COLA of 2.5 percent by reducing their annuity.

> Defined benefit plans are useful in attracting and retaining qualified employees. DC plans may appeal to younger and more mobile employees, but they are not as effective for retaining them. Cash balance plans are somewhere in the middle.

The State of Kansas. In 2012, the Kansas Legislature established its cash balance plan, in part to address its funding shortfall. The cash balance plan will apply to most new employees starting January 1, 2015, with the exception of correctional officers, who will be covered by the existing DB plan. Employees are required to contribute 6 percent of pay and the employer provides pay credits based on years of service according to the following schedule:

- 3 percent for 1-4 years.
- 4 percent for 5-11 years.
- 5 percent for 12-23 years.
- 6 percent for 24+ years.

Interest is credited on an employee's account balance at a guaranteed rate of 5.25 percent, with the possibility of an additional credit of up to 4 percent, based on the Kansas Public Employees Retirement System's investment returns and funded status. Employees are vested in their benefits after 5 years of service.

Employees are eligible for full retirement at age 65 with 5 years of service or age 60 with 30 years of service. Early retirement can begin at age 55 with 10 years of service, but with a reduced annual benefit. At retirement, an employee's account balance is annuitized to provide lifetime income. An employee retiring at full retirement age can take a partial lump-sum distribution of up to 30 percent of the account balance, with a reduced annuity. In addition, an employee can use the account balance to fund survivor benefits and a postemployment COLA with a reduced annuity. Disability benefits are paid as 60 percent of current salary. In-service death benefits include basic life insurance and the return of the member's contributions with interest. If the member has at least 5 years of service, the named spouse can choose to receive the account balance as an annuity, instead of as returned member contributions.

The State of Louisiana. In 2012, the Louisiana Legislature established a cash balance plan, which has since been successfully challenged in court.[2] Depending on the outcome of the appeal, beginning on or after July 1, 2013, the plan would be mandatory for newly hired members of the Louisiana State Employees' Retirement System, other than those in hazardous duty positions. The plan would also be mandatory for post-secondary education institution or management board members of the Teachers' Retirement System of Louisiana who do not elect to participate in the Optional Retirement Plan, a 401(k)-type plan. Members of the Louisiana School Employees' Retirement System and primary and secondary school members of TRSL could make an irrevocable election to join the cash balance plan. In each of the retirement systems, the cash balance plan would be a new tier of the existing defined benefit plan.

Under the plan, employees contribute 8 percent of pay, and employers contribute an actuarially required contribution. A cash balance plan member's account accumulates pay credits; 8 percent is funded by the employee contribution, and 4 percent is funded by the retirement system trust. Interest is credited on the employees' accounts at a rate that is one percentage point less than the retirement systems' actuarial rate of return, which is the annual rate of investment return based on the smoothed value of plan assets. The rate of credited interest may change from year to year; however, the employee's account can never be reduced should the rate fall below zero. Employees become vested in the 4 percent trust funded pay credit and interest credits once they have participated in the plan for 5 years. Employees who leave covered employment before they've participated for 5 years can only receive their employee contributions.

Employees are eligible to receive monthly retirement benefits at age 60 if they have participated in the plan for 5 or more years. The benefit is payable as a lifetime annuity, but a member can select optional forms of payment, including a lump-sum distribution with reduced annuity. Cash balance plan members and their survivors may elect to receive disability or survivor benefits available under the existing defined benefit plan of each system, if eligibility requirements are met.

LASERS and TRSL members are not covered by Social Security. The cash balance plan has been submitted to the Internal Revenue Service for a determination as to whether the plan meets social security equivalency requirements.

ADVANTAGES AND DISADVANTAGES

In considering the advantages and disadvantages of plan designs, the overall goals of both employers and employees need to be considered. For state and local government employers, key goals in providing retirement benefits include: 1) attracting and retaining qualified employees; and 2) providing sufficient and sustainable benefits. As discussed below, these goals are also important for state and local government employees, since they relate to the overall sufficiency of the benefits. The following discussion is summarized in Exhibit 3.

Attracting and Retaining Qualified Employees. Defined benefit plans are useful in attracting and retaining qualified employees. This is due to the rewards they provide for long-term service and their provision of guaranteed retirement, disability, survivor, and in-service death benefits. However, DB plans are generally less portable than DC plans and may not appeal as much to younger and more mobile employees. Although DC plans may appeal to such employees, they are not as effective for retaining them.

Cash balance plans are somewhere in the middle. Because the benefits accumulate as an account balance, they are more portable and may be appealing to more mobile employees. In addition, the account balance can be converted to an annuity upon retirement and, therefore, reward service with a guaranteed lifetime benefit. However, in themselves, cash balance plans may not provide attractive disability or survi-

Exhibit 3: Advantages and Disadvantages of Plan Designs

		Defined Benefit Plan	Defined Contribution Plan	Cash Balance Plan
Attract and Retain Qualified Employees	Advantages	• Rewards long-term service • Provides death and disability benefits	• May appeal to younger and more mobile employees	• May appeal to younger and more mobile employees
	Disadvantages	• Less portable than defined contribution benefits • May not appeal to more mobile employees	• May not be effective in retaining employees • Death and disability benefits only provided as distribution of DC account balance	• May not provide death and disability benefits
Sufficient and Sustainable Benefits	Advantages	• Provides guaranteed lifetime benefits • Pools risks related to investment, longevity, and inflation	• Gives members control over investment selection	• Provides guaranteed lifetime benefits • Pools risks related to investment, longevity and inflation
	Disadvantages	• Lower benefits to short-term employees than under a cash balance plan	• Transfers investment, longevity, and inflation risk to employees • Higher fees for investment administration and management	• Benefit sufficiency difficult to understand • Lower benefits to career employees than under a defined benefit plan

vor benefits. Also, since cash balance plans are more portable, they may be less effective than DB plans in retaining employees.

Providing Sufficient and Sustainable Benefits. Because DB plans provide benefits based on an employee's service and final average salary, the accumulated benefit is clear and directly related to replacing an employees' pre-retirement income. Moreover, because the benefit is provided as a guaranteed lifetime annuity, retired employees can count on the benefit over their lifetimes. However, since DB plans shift the risks of funding the benefit to the employer, the employer's contributions may be more volatile which could jeopardize sustainability. While DC plans limit the employer's contribution volatility by shifting these risks to employees, the benefits they provide are much less certain and may prove insufficient throughout retirement.

Cash balance plans may help mitigate the investment risks by managing the interest rate credited to the employee' accounts.

Cash balance plans may help mitigate the investment risks by managing the interest rate credited to the employee' accounts. If the interest is credited to employee accounts at a rate that reflects the plan's long-term rate of return, but also allows for adverse experience, the employer's contribution rates may be somewhat more stable. However, employers in cash balance plans are still subject to investment risks, since the interest credits promised to employees must be honored, even when the plan earns negative investment returns.

Longevity risk is the risk that employees may outlive their savings. The amount of longevity risk borne by the employer and employees can vary in a cash balance plan depending on how much of the benefit is paid as a lump sum, how much is annuitized, and how much of a subsidy or surcharge is applied to annuities.

However, because the benefit provided by a cash balance plan is expressed as an account balance rather than an annual benefit, it may be difficult for employees to judge whether it will be sufficient throughout retirement. In addition, the benefits provided by a cash balance plan for career employees may be substantially less than those provided by a final average salary DB plan of a similar contribution level, all else being equal. This is because the benefits provided by a cash balance plan are based on the employees' earnings over their full careers, rather than the earnings near the end of their careers.

CONCLUSIONS

The financial downturn and resulting economic decline have put many governments under fiscal stress. As a result, numerous state and local governments have recently made significant changes to their retirement plans in order to manage their costs including, in two very recent cases, establishing cash balance plans. However, if these new designs are used, care should be taken that the implications are fully understood and that they are effective in attracting and retaining qualified employees and providing sufficient and sustainable retirement benefits.

Notes

1. In addition, commissioned law enforcement employees also contribute an extra 1 to 2 percent of pay, depending on the size of the county's population. The counties match the additional law enforcement contributions at 100 percent.
2. In late January 2013, a district court ruled the cash balance plan to be unconstitutional. Under the Louisiana Constitution, a two-thirds vote is required for any changes to a public retirement system that have actuarial costs. While the cash balance plan obtained a majority of the vote, it fell short of the required two-thirds. Proponents of the plan will likely appeal the decision.

PAUL ZORN is director of governmental research at the benefit consulting and actuarial firm of Gabriel, Roeder, Smith & Company.

NASRA Issue Brief:
Public Pension Plan Investment Return Assumptions

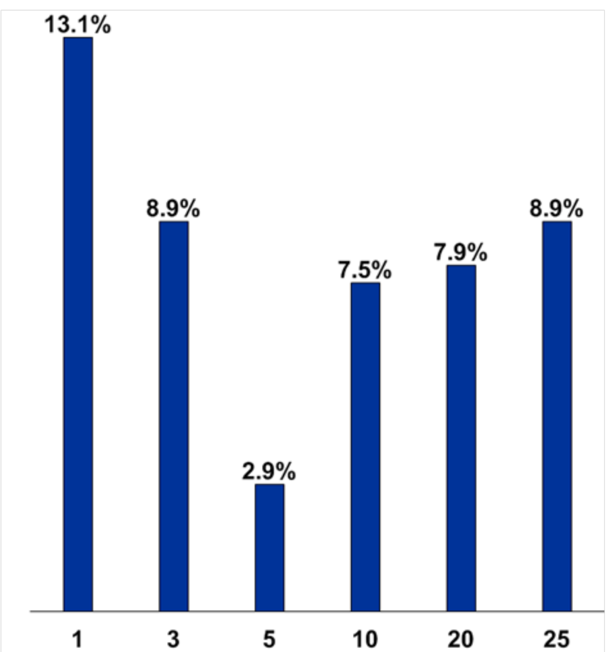
Updated March 2013

At year-end 2012, state and local government retirement systems held assets of approximately $3.05 trillion.[1] These assets are invested to defray the cost of benefits within an acceptable level of risk. The investment return on these assets matters because over time, investment earnings account for a majority of public pension fund revenues. A shortfall in expected investment earnings must be made up by higher contributions or reduced benefits.

Funding a pension benefit requires the use of projections, known as actuarial assumptions, about future events. Actuarial assumptions fall into one of two broad categories: demographic and economic. Demographic assumptions are those pertaining to a pension plan's membership, such as changes in the number of working and retired plan participants; when participants will retire, and how long they'll live after they retire. Economic assumptions pertain to such factors as the rate of wage growth and the investment return on the fund's assets.

As with other actuarial assumptions, projecting public pension fund investment returns requires a focus on the long-term. This brief discusses how investment return assumptions are established and evaluated and compares these assumptions with public funds' actual investment experience.

Figure 1: Median public pension annualized investment returns for period ended 12/31/12



Source: Callan Associates, Inc.

Public pension fund investment return assumptions have been the focus of growing attention in recent years. With current low current interest rates and volatile investment returns, some believe these assumptions are unrealistically high. Because investment earnings account for a majority of revenue for a typical public pension fund, the accuracy of the assumption has a major effect on the plan's finances and actuarial funding level.

An investment return assumption that is set too low will overstate liabilities and costs, causing current taxpayers to be overcharged and future taxpayers to be undercharged. A rate set too high will understate liabilities, undercharging current taxpayers, at the expense of future taxpayers. An assumption that is significantly wrong in either direction will cause a misallocation of resources and unfairly distribute costs among generations of taxpayers.

Although public pension funds, like other investors, have experienced sub-par returns over the past decade, median public pension fund returns over longer periods meet or exceed the assumed rates used by most plans. As shown in Figure 1, at 8.9 percent, the median annualized investment return for the 25-year period ended December 31, 2012, exceeds the most-used investment return assumption of 8.0 percent. The 10-year return is slightly below the average assumption of 7.77 percent (see Figure 4).

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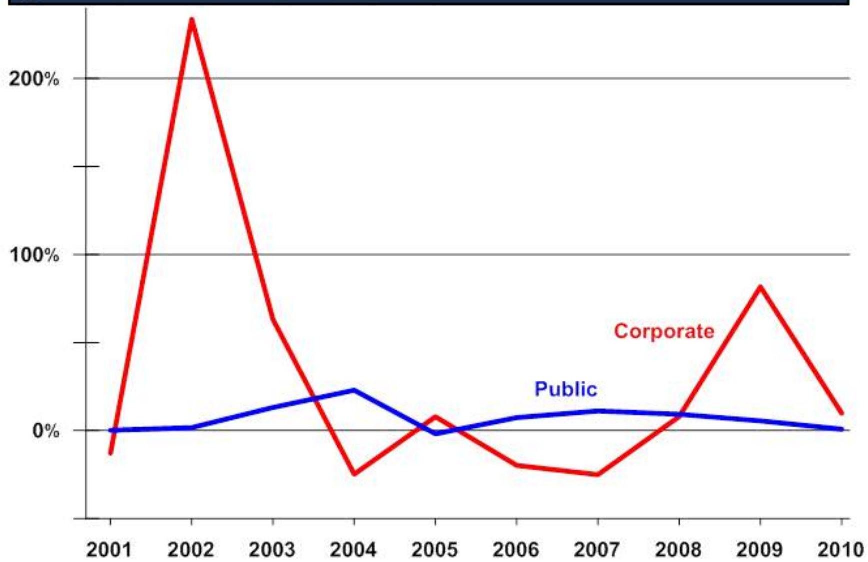
[1] Federal Reserve, *Flow of Funds Accounts of the United States: Flows and Outstandings, Fourth Quarter 2012*, Table L.117

Public retirement systems employ a process for setting and reviewing their actuarial assumptions, including the expected rate of investment return. Most systems review these assumptions regularly, pursuant to statute or system policy. The process for establishing and reviewing the investment return assumption involves consideration of various financial, economic, and market factors, and is based on a very long-term view, typically 30 to 50 years. A primary objective for using a long-term approach in setting the return assumption is to promote stability and predictability of cost.

Figure 2: Comparison of change from prior year in corporate and public pension contributions, 2001 to 2010



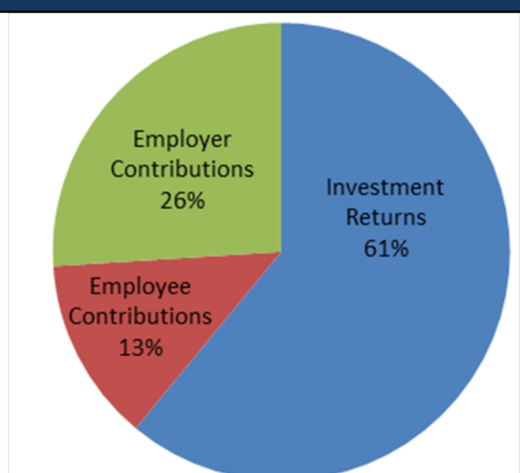
Source: Milliman and U.S. Census Bureau

Unlike public pension plans, corporate plans are required by federal regulations to make contributions on the basis of current interest rates. As Figure 2 shows, this method results in plan costs that are volatile and uncertain, often changing dramatically from one year to the next. This volatility is due in part to fluctuations in interest rates. This volatility has been identified as a leading factor in the decision among corporations to abandon their pension plans. By focusing on the long-term and relying on a stable investment return assumption, public plans experience less volatility of costs.

As Figure 3 shows, since 1982, public pension funds have accrued an estimated $4.8 trillion in revenue, of which $2.9 trillion, or 61 percent, is estimated to have come from investment earnings. Employer (taxpayer) contributions account for $1.3 trillion, or 26 percent of the total, and employee contributions total $623 billion, or 13 percent.

Public pension plans operate over long timeframes and manage assets for participants whose involvement with the plan can last more than half a century. Consider the case of a newly-hired public school teacher who is 25 years old. If this pension plan participant elects to make a career out of teaching school, he or she may work for 35 years, to age 60, and live another 25 years, to age 85. This teacher's pension plan will receive contributions for the first 35 years and then pay out benefits for another 25 years. During the entire 60-year period, the plan is investing assets on behalf of this participant. To emphasize the long-term nature of the investment return assumption, for a typical career employee, more than one-half of the investment income earned on assets accumulated to pay benefits is received *after* the employee retires.

Figure 3: Public Pensions Sources of Revenue, 1981-2011



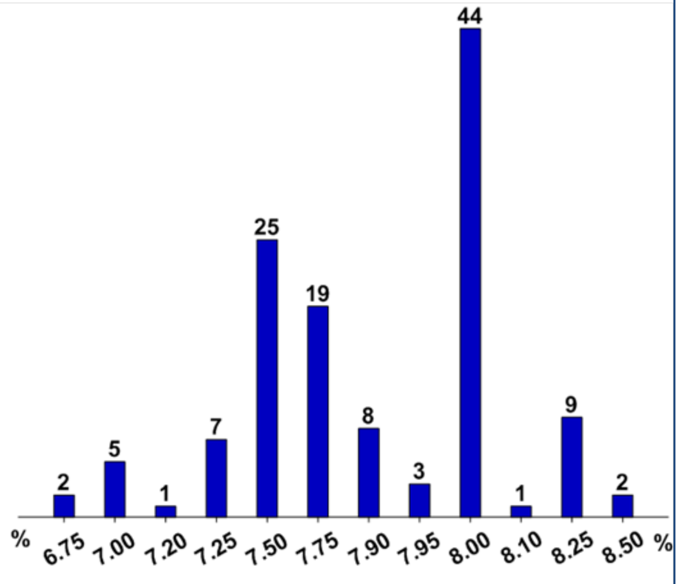
Source: U.S. Census Bureau

The investment return assumption is established through a process that considers factors such as economic and financial criteria; the plan's liabilities; and the plan's asset allocation, which reflects the plan's capital market assumptions, risk tolerance, and projected cash flows.

Standards for setting an investment return assumption, established and maintained by professional actuaries, recommend that actuaries consider a range of specified factors, including current and projected interest rates and rates of inflation; historic and projected returns for individual asset classes; and historic returns of the fund itself. The investment return assumption reflects a value within the projected range.

Many public pension funds have reduced their return assumption in recent years. Among the 126 plans measured in the Public Fund Survey (see Figure 4), nearly one-half have reduced their investment return assumption since fiscal year 2008. While 8.0 percent remains the predominant rate assumption, the average is 7.77 percent. Appendix A details the assumptions in use or adopted by the 126 plans in the Public Fund Survey.

Figure 4: Distribution of investment return assumptions



Public Fund Survey March 2013

Conclusion

Since 1987, a period that has included three economic recessions and four years when median public pension fund investment returns were negative (including the 2008 decline), public pension funds have exceeded their assumed rates of investment return. Changes in economic and financial conditions are causing many public plans to reconsider their investment return assumption. Such a consideration must remain consistent with the long timeframe under which plans operate.

See Also:

Actuarial Standards of Practice No. 27, Actuarial Standards Board, http://www.actuarialstandardsboard.org/pdf/asops/asop027_109.pdf

The Liability Side of the Equation Revisited, Missouri SERS, September 2006, http://www.mosers.org/~/media/Files/Adobe_PDF/About_MOSERS/Board-Newsletters/Operations-Outlook/operations_outlook_September06.ashx

The Public Fund Survey is sponsored by the National Association of State Retirement Administrators and the National Council on Teacher Retirement, http://www.publicfundsurvey.org (registration required)

Contact:

Keith Brainard, Research Director
keithb@nasra.org

Alex Brown, Research Associate
alexbrown@nasra.org

National Association of State Retirement Administrators
www.nasra.org

Appendix A: Investment Return Assumption by Plan

(Figures reflect the nominal assumption in use or announced for use as of March 2013)

Alabama ERS	8.00%
Alabama Teachers	8.00%
Alaska PERS	8.25%
Alaska Teachers	8.25%
Arizona Public Safety Personnel	8.00%
Arizona SRS	8.00%
Arkansas PERS	8.00%
Arkansas Teachers	8.00%
California PERS	7.50%
California Teachers	7.50%
Chicago Teachers	8.00%
City of Austin ERS	7.75%
Colorado Affiliated Local	7.75%
Colorado Fire & Police Statewide	7.75%
Colorado Municipal	8.00%
Colorado School	8.00%
Colorado State	8.00%
Connecticut SERS	8.25%
Connecticut Teachers	8.50%
Contra Costa County	7.25%
DC Police & Fire	7.00%
DC Teachers	7.00%
Delaware State Employees	7.50%
Denver Employees	8.00%
Denver Public Schools	8.00%
Duluth Teachers [1]	8.00%
Fairfax County Schools	7.50%
Florida RS	7.75%
Georgia ERS	7.50%
Georgia Teachers	7.50%
Hawaii ERS	7.75%
Houston Firefighters	8.50%
Idaho PERS	7.00%
Illinois Municipal	7.50%
Illinois SERS	7.75%
Illinois Teachers	8.00%
Illinois Universities	7.75%
Indiana PERF	6.75%
Indiana Teachers	6.75%
Iowa PERS	7.50%
Kansas PERS	8.00%
Kentucky County	7.75%
Kentucky ERS	7.75%
Kentucky Teachers	7.50%
LA County ERS	7.75%
Louisiana SERS	8.00%
Louisiana Teachers	8.25%
Maine Local	7.25%
Maine State and Teacher	7.25%
Maryland PERS	7.75%
Maryland Teachers	7.75%
Massachusetts SERS	8.25%
Massachusetts Teachers	8.25%
Michigan Municipal	8.00%
Michigan Public Schools	8.00%
Michigan SERS	8.00%
Minnesota PERF [1]	8.00%
Minnesota State Employees [1]	8.00%
Minnesota Teachers [1]	8.00%
Mississippi PERS	8.00%
Missouri DOT and Highway Patrol	8.25%
Missouri Local	7.25%
Missouri PEERS	8.00%
Missouri State Employees	8.00%
Missouri Teachers	8.00%
Montana PERS	7.75%
Montana Teachers	7.75%
Nebraska Schools	8.00%
Nevada Police Officer and Firefighter	8.00%
Nevada Regular Employees	8.00%
New Hampshire Retirement System	7.75%
New Jersey PERS	7.95%
New Jersey Police & Fire	7.95%
New Jersey Teachers	7.95%
New Mexico PERF	7.75%
New Mexico Teachers	7.75%
New York City ERS	8.00%
New York City Teachers	8.00%
New York State Teachers	8.00%
North Carolina Local Government	7.25%
North Carolina Teachers and State Employees	7.25%
North Dakota PERS	8.00%
North Dakota Teachers	8.00%
NY State & Local ERS	7.50%

NY State & Local Police & Fire	7.50%
Ohio PERS	8.00%
Ohio Police & Fire	8.25%
Ohio School Employees	7.75%
Ohio Teachers	7.75%
Oklahoma PERS	7.50%
Oklahoma Teachers	8.00%
Oregon PERS	8.00%
Pennsylvania School Employees	7.50%
Pennsylvania State ERS	7.50%
Phoenix ERS	8.00%
Rhode Island ERS	7.50%
Rhode Island Municipal	7.50%
San Diego County	8.00%
San Francisco City & County [3]	7.50%
South Carolina Police	7.50%
South Carolina RS	7.50%
South Dakota PERS[4]	7.25%
St. Louis School Employees	8.00%
St. Paul Teachers [1]	8.00%
Texas County & District	8.00%
Texas ERS	8.00%
Texas LECOS	8.00%
Texas Municipal	7.00%
Texas Teachers	8.00%
TN Political Subdivisions	7.50%
TN State and Teachers	7.50%
Utah Noncontributory	7.75%
Vermont State Employees [2]	8.10%
Vermont Teachers [2]	7.90%
Virginia Retirement System	7.00%
Washington LEOFF Plan 1	7.90%
Washington LEOFF Plan 2	7.90%
Washington PERS 1	7.90%
Washington PERS 2/3	7.90%
Washington School Employees 2/3	7.90%
Washington Teachers Plan 1	7.90%
Washington Teachers Plan 2/3	7.90%
West Virginia PERS	7.50%
West Virginia Teachers	7.50%
Wisconsin Retirement System	7.20%
Wyoming Public Employees	8.00%

1. The Minnesota Legislature, which sets in statute investment return assumptions used by public plans in the state, established the use of “select-and-ultimate” rates for investment return assumptions. These plans will use an assumed rate of 8.0 percent for five years, through FY 16, then return to 8.5 percent. For more information on select-and-ultimate rates, please see Actuarial Standards of Practice No. 27: http://www.actuarialstandardsboard.org/pdf/asops/asop027_145.pdf.

2. The Vermont retirement systems adopted “select-and-ultimate” rates in 2011; the rates shown reflect the single rates most closely associated with the funding results for the respective plans, based on their projected cash flows.

3. The SDRS set the rate at 7.25% through FY 2018, after which it will rise to 7.50%.

PENSION FUNDING:

A Guide for Elected Officials

Report from the Pension Funding Task Force 2013

Issued by:

National Governors Association (NGA)
National Conference of State Legislatures (NCSL)
The Council of State Governments (CSG)
National Association of Counties (NACo)
National League of Cities (NLC)
The U.S. Conference of Mayors (USCM)
International City/County Management Association (ICMA)
National Council on Teacher Retirement (NCTR)
National Association of State Auditors, Comptrollers and Treasurers (NASACT)
Government Finance Officers Association (GFOA)
National Association of State Retirement Administrators (NASRA)

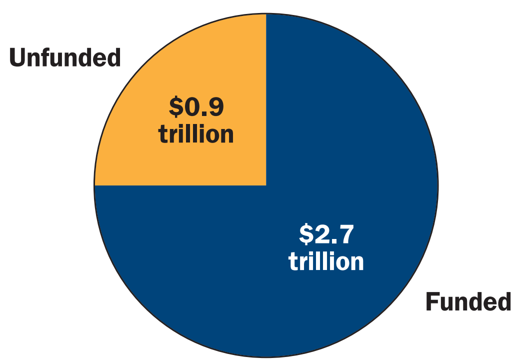
PENSION FUNDING:

A Guide for Elected Officials

Introduction

Defined benefit pension plans have a long history in public sector compensation. These plans are typically funded through a combination of employer and employee contributions and earnings from investments. Public pension plans hold more than $3 trillion in assets in trust on behalf of more than 15 million working and 8 million retired state and local government employees and their surviving family members. The pie chart below illustrates the 2011 funded status of 109 state-administered plans and 17 locally administered plans. These plans represent 85 percent of total state and local government pension assets and members.

Figure 1. *Funding of Aggregate Pension Liability, 2011*



Source: BC-CRR Estimates based on *Public Plans Database* (PPD).

The value of securities held by public and private retirement plans declined significantly following the economic crisis of 2008–2009, causing an increase in unfunded pension liabilities. The range of those unfunded public pension liabilities varies widely among governments. These same governments also have enacted major changes in their retirement plans over the past decade. Today, some public pension plans are well funded, while others have seen their funded status decline.

Now another change is on the horizon: new pension accounting standards issued by the Governmental Accounting Standards Board (GASB) in 2012. GASB Statement No. 67, *Financial Reporting for Pension Plans,* takes effect for pension plan fiscal years beginning after June 15, 2013 (fiscal years ending on or after June 30, 2014). GASB Statement No. 68, *Accounting and Reporting for Pensions,* applies to employers (and contributing nonemployers) in fiscal years beginning after June 15, 2014 (fiscal years ending on or after June 30, 2015).

These new accounting standards will change the way public pensions and their sponsoring governments report their pension liabilities. In particular, the new standards no longer provide guidance on how to calculate the actuarially determined annual required contribution (ARC), which many governments have used not only for accounting, but also to budget their pension plan contribution each year. In fact, these new GASB accounting standards end the relationship between pension accounting and the funding of the ARC.

In addition to GASB's new accounting standards, policymakers should be aware that rating agencies such as Moody's may use yet another set of criteria to assess the impact of pension obligations on the creditworthiness of a municipal bond issuer. If the ratings agencies publicize their pension calculations, state and local officials would be faced with the challenge of interpreting three sets of pension numbers: an accounting number to comply with the GASB's financial reporting requirements, an actuarial calculation to determine funding requirements for budgeting purposes, and a financial analysis figure produced by bond rating agencies to evaluate and compare issuers of municipal debt.

This guide provides key facts about public pension plans, why it is essential to have a pension funding policy, a brief overview of the new GASB standards, and which issues state and local officials need to address. The guide also offers guidance for policy makers to use when developing their pension plan's funding policy.

Pension funding background

In the 1970s, it was not uncommon for state and local governments to fund their pensions on a pay-as-you-go basis. Following the passage of ERISA, which set private sector funding requirements, state and local officials took steps to fully advance-fund their pensions. They were further encouraged to meet their actuarial funding obligations by new accounting and reporting standards issued by the GASB in 1986.

The trend to improve pension funding continued over the next decade. When the GASB issued Statements 25 and 27 in 1994, employers were required to disclose information on plan assets and liabilities in their financial reports. More important, to comply with GASB, employers also had to disclose their actuarially determined ARC and the percentage of the ARC the employer actually paid. The GASB defined the ARC to include the normal cost of pensions for today's employees plus a contribution to pay for any unfunded liabilities, typically amortized over a maximum 30-year period. Paying the full ARC has been an important measure of whether or not a pension plan is on track to fund its pension promises.

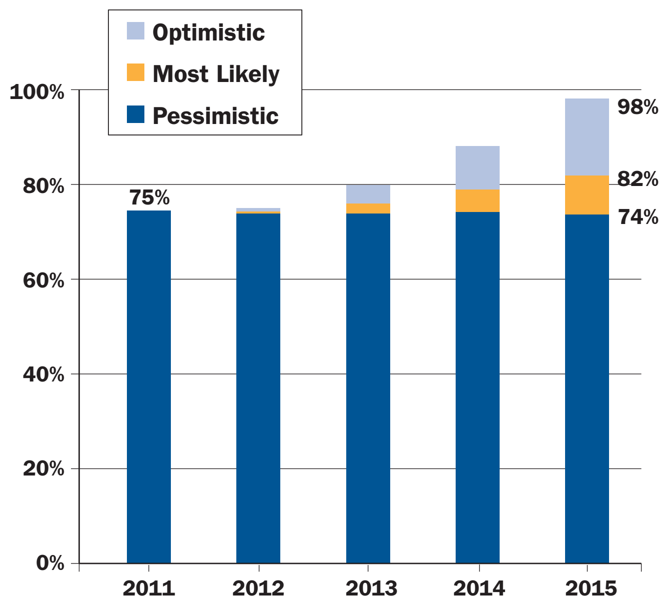
By the turn of the century, public pensions were as well funded as private pensions. In fact, most public plans were nearly 100 percent funded in 2000. Unfortunately, the last decade of economic upheaval and the wide swings in the stock market have reduced pension assets in both public and private plans.

In 2011, the estimated aggregate ratio of assets to liabilities slipped to 75 percent[1]. State and local officials have stepped up their efforts to restore pension funding. According to the National Conference of State Legislatures, 44 states have enacted major changes in state retirement plans from 2009–2012.[2] Changes have included increases in employee contributions to pension plans, longer vesting periods, reduced benefit levels, higher retirement ages, and lower cost-of-living adjustments. Some modifications may apply to new workers only, while others affect current employees and/or retirees.

Pension funding policies

A variety of state and local laws and policies guide decisions concerning pension funding practices. Many state and local governments have passed legislation that stipulates how pensions should be funded. Others have policies that address how pension assets are to be invested or if pension reserves must be maintained.

Figure 2. *Projected State and Local Funding Ratios Under Three Scenarios, 2011–2015*



Source: BC-CRR estimates for 2011–2015 based on *Public Plans Database* (PPD).

Generally speaking, employers with well-funded pension plans take a long-term approach to estimating investment returns, adjust their demographic and other assumptions as needed, and consistently pay their annual required contribution in full.

A clear pension funding policy is important because it:

- Lays out a plan to fund pensions;
- Provides guidance in making annual budget decisions;
- Demonstrates prudent financial management practices;
- Reassures bond rating agencies; and
- Shows employees and the public how pensions will be funded.

GASB's new approach

Under prior GASB statements, there was a close link between accounting and funding measures. That link has now been broken. The new GASB standards

1 Munnell, Alicia H., Aubrey, Jean-Pierre, Hurwitz, Josh, Medinica, Madeline, and Quinby, Laura, "The Funding of State and Local Pensions: 2011–2015," Center for State and Local Government Excellence, May 2012.

2 Snell, Ron, "State Retirement Legislation 2009–2012," National Conference of State Legislatures, July 31, 2012.

focus entirely on accounting measurements of pension liabilities and no longer on how employers fund the cost of benefits or calculate their ARC. This is a significant change for government employers because the ARC historically served as a guide for policy makers, employees, bond rating agencies and the public to determine whether pension obligations were being appropriately funded. The ARC also often was used to inform budget decisions.

Today, employers report a liability on the face of their financial statements only if they fail to fully fund their ARC (just as a homeowner would report a liability only for mortgage payments in arrears). Thus, many government employers today do *not* report a liability for pensions on the face of their financial statements. However, if the plan they sponsor does have an unfunded pension liability, it is reported in the notes to the financial statements, which are considered an integral part of financial reporting. In contrast, under the new GASB standards, employers will report their unfunded pension liability on the face of their financial statements, even if they fully fund each year's ARC (just as a homeowner would report a mortgage liability even if all monthly mortgage payments are paid on time, in full). Thus, in the future, all employers will report any unfunded pension liability on the face of their financial statements, and that amount may be substantial for many.

Furthermore, those seeking to know how much an employer should be contributing each year to the pension plan and how much the employer actually contributed (funding information) today can find that information in the employer's financial report. In contrast, under the new GASB pension accounting standards, employers will no longer *automatically* be required to obtain an actuarially determined ARC and then include information concerning that amount and actual employer contributions in their financial report.

Filling the gap in funding guidance

Because the GASB's new standards focus entirely on how state and local governments should account for pension liabilities and no longer focus on how employers fund the costs of benefits or calculate their ARC, a new source of guidance is needed.

To help fill that gap, the national associations representing local and state governments established a Pension Funding Task Force (Task Force) to develop policy guidelines.

The "Big 7" (National Governors Association, National Conference of State Legislatures, Council of State Governments, National Association of Counties, National League of Cities, U.S. Conference of Mayors, and the International City/County Management Association) and the Government Finance Officers Association established a pension funding task force in 2012. The National Association of State Auditors, Comptrollers and Treasurers; the National Association of State Retirement Administrators; and the National Council on Teacher Retirement also serve on it. The Center for State and Local Government Excellence is the convening organization for the Task Force.

The Task Force has monitored the work of the actuarial community and the rating agencies, as well as considered recommendations from their own organizations to develop guidelines for funding standards and practices and to identify methods for voluntary compliance with these standards and practices.

The actuarial and finance communities have been working on the pension funding issues and will be invaluable resources as governments make needed changes. Indeed, the California Actuarial Advisory Panel and the Government Finance Officers Association have issued guidelines consistent with the Task Force's recommendations, but with a greater level of specificity. The Conference of Consulting Actuaries is also preparing similar guidance. State and local officials are encouraged to review the guidelines and best practices of these organizations.

It also is important to note that some governments with well-funded pension plans will determine that they need to make few, if any, changes to their funding policies, while others may face many challenges. Keep in mind that changes can be made over time. A transition plan can address changes that may need to be phased in over a period of years. For example, an employer or retirement board that currently amortizes its unfunded liabilities over 30 years could adopt a transition plan to continue that schedule (as a fixed, decreasing period) for current unfunded liabilities and to amortize any new unfunded liabilities over 25 years. In five years, that pension plan would have completed its transition to a 25-year amortization period.

In many cases, governments will need to strike a balance between competing objectives to determine the most appropriate timeframe in which to meet their goals.

Task force recommendations

States and localities have established distinct statutory, administrative and procedural rules governing how retirement benefits are financed. While nothing in the new GASB standards or the possible credit rating agency changes *requires* a change in funding policy, the Task Force recommends pension funding policies be based on the following five general policy objectives:

1. Have a pension funding policy that is based on an actuarially determined contribution.
2. Build funding discipline into the policy to ensure that promised benefits can be paid.
3. Maintain intergenerational equity so that the cost of employee benefits is paid by the generation of taxpayers who receives services.
4. Make employer costs a consistent percentage of payroll.
5. Require clear reporting to show how and when pension plans will be fully funded.

A sound pension funding policy should address at least the following three core elements of pension funding in a manner consistent with the policy objectives:

- Actuarial cost method;
- Asset smoothing method; and
- Amortization policy.

These core elements should be consistent with the parameters established by GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, with which most governmental entities currently comply. Such parameters specify an actuarially determined ARC that should comply with applicable Actuarial Standards of Practice (ASOP No. 4), be based on an estimated long-term investment yield for the plan, and should amortize unfunded liabilities over no more than 30 years. The actuarially determined ARC, the parameters for determining the ARC, and the percentage of the ARC the employer actually paid should be disclosed and reassessed periodically to be sure that they remain effective. To that end, the Task Force recommends that state and local governments not only stay within the ARC calculation parameters established in GASB 27, but also consider the following policy objectives when reviewing each core element of their funding policy:

Actuarial Cost Method: the method used to allocate the pension costs (and contributions) over an employee's working career.

Policy Objectives:

1. Each participant's benefit should be fully funded under a reasonable allocation method by the expected retirement date.
2. The benefit costs should be determined as a level percentage of member compensation and include expected income adjustments.

The Entry Age Normal (level percentage of payroll) actuarial cost method is especially well-suited to meeting these policy objectives.

Asset Smoothing Method: the method used to recognize gains or losses in pension assets over some period of time to reduce the effects of market volatility and provide stability to contributions.

Policy Objectives:

1. The funding policy should specify all components of asset smoothing, such as the amount of return subject to smoothing and the time period(s) used for smoothing a specific gain or loss.
2. The asset smoothing method should be the same for both gains and losses and should not be reset or biased toward high or low investment returns.

The use of a five-year period for "smoothing" investment experience is especially well-suited to meeting these policy objectives.

Amortization Policy: the policy that determines the length of time and structure of payments required to systematically fund accrued employee benefits not covered by the actuarial value of assets.

Policy Objectives:

1. The adjustments to contributions should be made over periods that appropriately balance intergenerational equity against the goal of keeping contributions level as a percentage of payroll over time.
2. The amortization policy should reflect explicit consideration of (a) gains and losses actually experienced by a plan, (b) any changes in assumptions and methods, and (c) benefit or plan changes.
3. The amortization of surplus requires special consideration consistent with the goal of stable costs and intergenerational equity.

Amortizing the various components of the unfunded actuarial accrued liability over periods that focus on matching participant demographics but also, except for plan amendments, consider managing contribution volatility, is especially well-suited to meeting these policy objectives.

Conclusion

The most important step for local and state governments to take is to base their pension funding policy on an actuarially determined contribution (ADC). The ADC should be obtained on an annual or biannual basis. The pension policy should promote fiscal discipline and intergenerational equity, and clearly report when and how pension plans will be fully funded.

Other issues to address in the policy are periodic audits and outside reviews. The ultimate goal is to ensure that pension promises can be paid, employer costs can be managed, and the plan to fund pensions is clear to everyone.

Resources

1. GFOA best practice, *Guidelines for Funding Defined Benefit Pension Plans*, at: www.gfoa.org
2. GASB Statements No. 67 and 68 at: www.GASB.org
3. GASB Statement 27: http://www.gasb.org/cs/ContentServer?site=GASB&c=Document_C&pagename=GASB%2FDocument_C%2FGASBDocumentPage&cid=1176160029312
4. Moody's Request for Comments: Adjustments to US State and Local Government Reported Pension Data at: http://www.wikipension.com/wiki/Moodys_Request_For_Comments
5. National Conference of State Legislatures, changes to state pension plans at: http://www.ncsl.org/documents/employ/2012-LEGISLATION-FINAL-Aug-31-2012.pdf
6. The National Association of State Retirement Administrators for examples of state funding policies at: www.NASRA.org
7. Center for State and Local Government Excellence for examples of changes to state and local government pension plans at: http://slge.org
8. California Actuarial Advisory Panel at: http://www.sco.ca.gov/caap.html
9. Conference of Consulting Actuaries at: http://www.ccactuaries.org/index.cfm

For More Information

National Governors Association
Barry Anderson ▪ (202) 624-5318, banderson@nga.org

National Conference of State Legislatures
Michael Bird ▪ (202) 624-8686, michael.bird@ncsl.org
Jeff Hurley ▪ (202) 624-7753, jeff.hurley@ncsl.org

The Council of State Governments
Chris Whatley ▪ (202) 624-5460, cwhatley@csg.org

National Association of Counties
Deseree Gardner ▪ (202) 942-4204, dgardner@naco.org

National League of Cities
Neil Bomberg ▪ (202) 626-3042, bomberg@nlc.org

The U.S. Conference of Mayors
Larry Jones ▪ (202) 861-6709, ljones@usmayors.org

International City/County Management Association
Joshua Franzel ▪ (202) 682-6104, jfranzel@icma.org

Center for State and Local Government Excellence
Elizabeth Kellar ▪ (202) 962-3611, ekellar@slge.org

National Association of State Auditors, Comptrollers and Treasurers
Cornelia Chebinou ▪ (202) 624-5451, cchebinou@nasact.org

Government Finance Officers Association
Barrie Tabin Berger ▪ (202) 393-8467, btberger@gfoa.org

National Association of State Retirement Administrators
Jeannine Markoe Raymond ▪ (202) 624-1417, jeannine@nasra.org

National Council on Teacher Retirement
Leigh Snell ▪ (540) 333-1015, lsnell@nctr.org