

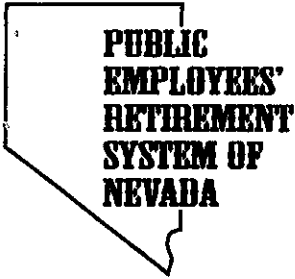
DISCLAIMER

Electronic versions of the exhibits in these minutes may not be complete.

This information is supplied as an informational service only and should not be relied upon as an official record.

Original exhibits are on file at the Legislative Counsel Bureau Research Library in Carson City.

Contact the Library at (775) 684-6827 or library@lcb.state.nv.us.



Assembly Government Affairs Committee
PERS' Orientation Testimony
February 7, 2003 - 8:30 a.m. - Room 3143

RETIREMENT BOARD

CHARLES A. SILVESTRI
Chairman
SUE DEFRANCESCO
Vice Chairman

Members

L. MARK BALEN
PURISMO B. HERNANDEZ
DAVID F. KALLAS
MARVIN A. LEAVITT
WARREN WISH

EXECUTIVE STAFF

GEORGE PYNE
Executive Officer

DANA K. BILYEU
Operations Officer

LAURA B. WALLACE
Investment Officer

693 W. Nye Lane
Carson City, Nevada
89703
(775) 687-4200
Fax: (775) 687-5131

5820 S. Eastern Avenue
Suite 220
Las Vegas, Nevada
89119
(702) 486-3900
Fax: (702) 678-8934

Website: www.nvpers.org

Mr. Chairman, members of the committee, my name is George Pyne. I am the Executive Officer of the Public Employees' Retirement System. With me today are the System's Operations Officer, Dana Bilyeu, and Investment Officer, Laura Wallace.

On the second page of your packet, we provided you with a list of areas we are going to cover in our overview of the Public Employees' Retirement System (PERS), more commonly known as PERS. These items include our mission, history, administrative structure in which we operate, legal obligations of our plan and plan design, our investment program, funding, a brief look at our legislative agenda for 2003, the Legislators' Retirement System, and the Judicial Retirement System.

The mission of PERS is stated at NRS 286.015. It states that ...*"the purpose of PERS is to provide a reasonable base income to our public employees whose earning capacity has been reduced on account of age or disability."* PERS' mission is further defined as ...*"a system which will make government employment attractive to qualified employees and encourage them to remain in government service to give the public employer and the public the full benefit of their training and experience."*

Next, Dana will review PERS' history, plan design, administrative structure, and legal obligations.

ORIGINALS ARE ON FILE IN
THE RESEARCH LIBRARY

ASSEMBLY GOVERNMENT AFFAIRS
DATE: 2-7-03 ROOM: 3143 EXHIBIT C
SUBMITTED BY: Geo. Pyne, EO, PERS
PAGE 1 of 11

Thank you George. Mr. Chairman, members of the committee, for the record I am Dana Bilyeu, Operations Officer for PERS.

PERS History (Page 4)

The System was established in 1947 partially in response to the fact that public workers at that time were prevented from participating in the Social Security System. The approach to retirement security for public workers was very piecemeal in our state in that some public employers had retirement benefits and some did not. Over the course of a few years all the systems were consolidated and PERS was born.

In 1967, the Legislators' Retirement System was implemented and provides a benefit formula of 25\$ per year of service.

In 1971, the legislature recognized that, while the benefit structure, as it was built over the course of time delivered a reasonable base benefit for retirees of the System, the funding mechanism lagged. Recognizing this funding issue, the legislature commissioned an independent study of PERS. The study was delivered to the 1973 session and recommended a series of changes to how PERS was managed. The System moved to full actuarial funding meaning the contribution rate paid by employers and employees recognizes the costs of benefits to be paid. Monies are set aside today to fund future benefits. George will review that more in a moment.

The Constitution was amended to create the trust fund thus insuring the use of the funds solely for purposes directly related to the best interests of the members and beneficiaries. This essential protection was further expanded in 1996, by the passage of Question 1 which placed further safeguards in the Constitution and I will talk more about that in a moment.

Finally, the study indicated that as a multiple employer plan, the System owes equal duties to all employers and employees and therefore needed to be independent from any one single employer. The legislature passed certain statutes providing PERS with independence from State Government so that the State could not exert more influence over the plan than other employers could. This becomes important when you realize that the State is not even the largest employer participating in the System, that honor goes to the Clark County School District, by almost 8,000 employees. The legislature retained oversight over the System, and the Interim Retirement and Benefits Committee provides this oversight in the interim. PERS' budget is approved by the legislature as well.

In 1977, the police/fire fund was created in support of the public policy of promoting a youthful and vigorous front line police and fire force. That public policy still supports the early retirement provisions of this fund today.

Finally, the Judicial Retirement System was created to insure that judges' retirement was administered in like fashion to PERS and is funded on an actuarial reserve basis.

Turning the page, we have briefly highlighted PERS' management structure for your review. The structure is corporate in nature, but with a public twist. The System is governed by the 7-member Board of Trustees appointed by the Governor. The members of the Board are representative of the employers, members and retirees of the fund. The Executive Officer, Operations Officer and Investment Officer run the daily business of the agency. George is responsible for all agency decisions while Laura's responsibility is with oversight of the System's Investment Program. I manage the operations of the agency with the four

principle divisions listed. Employer and production services are responsible for wage and contribution reporting, as well as all calculations performed by the agency. Member and Retiree Services is responsible for counseling, telephone counseling, all educational programs, all publications, videos etc. The Accounting Division keeps the books for the system and provides daily interface with our banking institutions and Information Technology supports the computer infrastructure of PERS.

Moving to the next slide—(Page 6)

PERS is a creature of the Nevada Constitution and of statute. It is a constitutionally created trust fund found in Article 9 Section 2 which provides that any money paid for the purpose of funding and administering the Public Employees' Retirement System must be segregated and such money must never be used for any other purpose and is declared to be a trust fund. As I indicated a moment ago in 1996, the voters expanded this constitutional protection for the pension system by adding safeguarding language designed to prevent raids on the trust fund. These protections include:

- ◆ Requiring that the pension system be run by the Retirement Board
- ◆ That the Retirement Board be the hiring authority for the executive officer
- ◆ That the Retirement System employ an independent actuary
- ◆ The board shall adopt assumptions based upon the recommendation made by the independent actuary it employs
- ◆ PERS can not invest in obligations of the State or loan money to the State

Additionally, just a quick point about the nature of the pension benefit. Through the contract clauses of the U.S. Constitution and the Nevada Constitution, the pension benefit is part of the employment contract and therefore vests in an employee from the first day of employment. The pension structure that was in existence on the first day of public employment can not be diminished without replacing the benefit with one of equal or greater value.

Finally, in order for the trust fund to function in a tax deferred manner the plan document, meaning our statute, must comply with certain provisions of the Internal Revenue Code. That is why if you reviewed Chapter 286, the Retirement Act, you would see all sorts of reference to the Internal Revenue Code, putting into place certain benefit restrictions, as well as forfeiture restrictions etc. These provisions are mandatory to insure operation of the fund is done on a tax-deferred basis.

Very briefly (page 7), PERS is a 401(a) defined benefit plan which simply means that benefits from this program are definitely determinable by the application of a statutory formula. If you turn to the next page, you will see that statutory formula and an example of how the formula works.

There are three basic components to your retirement calculation. First, your years of service credit. Second, what we call the service time multiplier that for ease in our example we have used 2.5%. Third, your average compensation, figured by taking the average of your highest consecutive 36 months of pay. Looking at the example, you will see how the formula works.

For purposes of receiving a benefit from PERS, a member must have at least 5 years of public service. Retirement eligibility ages are set forth for both the regular plan as well as the police and fire plan.

Finally, PERS also administers two other programs: disability retirement and a survivor benefit program.

Thank you Dana. For the record, George Pyne. On page 8 in your handout, we address how PERS' benefits are funded. Money for the payment of benefits comes from two sources, contributions made by employees and employers and return on investments. Interestingly enough, up to 80% of the benefits paid to a typical PERS' retiree comes from return on investments. This shows just how important PERS' investment program is in financing the benefits of our members and retirees.

PERS is funded on an actuarial reserve basis. Put simply, contributions are set aside today and invested to pay for expected future benefits. This is unlike the Social Security system where benefits are funded on a pay as you go basis. This means, today's workers are financing the benefits of today's retirees.

Today PERS is 82% funded (page 9), which means we have 82 cents on hand for each dollar of liabilities. The Board established a funding schedule to pay off the System's unfunded liabilities over a 40-year period beginning in 1984. PERS was 55% funded at that time. Full funding is expected in 2024.

PERS has two contribution plans, the employee/employer joint contribution plan (EES/ERS) (page 10) and the employer pay plan (EPC) (page 11). Under the employee/employer plan the employee presently contributes 9.75% of his pay as a regular member or 14.75% as a police/fire member, on an after tax basis into PERS. The public employer matches the employee's contribution. About 20% of PERS' membership participates under this contribution program.

Other PERS' members contribute under the employer pay contribution plan (EPC). The EPC plan started in 1975. It was passed by the Nevada Legislature to

provide a cost savings to Nevada public employers and an increase in take-home pay to public employees.

Under EPC, the public employer and employee share equally in the cost of retirement. Payment of the employee's portion of the retirement contributions by the public employer must be:

- Made in lieu of equivalent pay increases; or
- Counterbalanced by equivalent reductions in employees' salaries.

Contribution rates by statute are scheduled to increase July 1, 2003, for regular members while police/fire rates will remain at their present levels. The following two exhibits show the current rates and rates effective July 1, 2003. Statutory rates of contribution must change if the difference between the rates in the latest actuarial valuation and statutory rates is greater than .5%.

The next page (12) shows our projection of the near future, as well as a look back at the past. As you can see, PERS has experienced tremendous growth in both members and benefit recipients since 1976 and will likely grow at a fast pace in the near future. The ratio of members to benefit recipients shows the importance of funding our plan on a current basis. If reserves were not set aside today to pay for future benefits, you can imagine the contribution rates future generations would need to pay to fund the benefits of today's workers.

Next I'd like to review your benefits under the Legislators' Retirement System (LRS) (page 13). The LRS was created in 1967 to provide legislators with retirement and survivor benefits. Like PERS, it is a defined benefit plan which means your benefit is based on a formula tied to your age and years of service at retirement.

As a legislator, you are eligible to receive an unreduced benefit at age 60 with 10 or more years of service. For each year of service you receive \$25.00 monthly at retirement. Therefore, a legislator who retires at age 60 with 10 years of service can expect to receive a pension of \$250.00 per month. There are various optional forms of payment that would provide you with a reduced amount at retirement in order to provide your beneficiary with an ongoing benefit after your death. Post retirement increases (PRI's) are paid in the same manner as PERS' members.

The LRS today is 72% funded (page 14) and is on the same amortization schedule as PERS with full funding expected in 2024. Benefits are funded through contributions received by you and the State of Nevada as your employer. Your contribution amount is 15% of your pay which is refundable to you if you don't retire. The State of Nevada pays an annual contribution amount which is actuarially determined to be sufficient to fund future benefits.

The new JRS was established in 2001. It is presently 21% funded with full funding expected in 2037. Prior to 2001, this was an unfunded pay as you go plan funded directly by contributions from the State General Fund.

Next I'd like to mention PERS' legislative program for 2003 (page 15). We do not have a fiscal impact bill, but we do have a technical or housekeeping bill, BDR-563. PERS' bill draft request makes several definitional and clarification changes to the Public Employees' Retirement Act and the Judicial Retirement Act, it also modifies language at NRS 286.523 with regard to reemployed retirees. This recommended change restricts exemption from PERS' reemployment restrictions for critical labor shortage positions to 2-years for retirees who are hired in those positions beginning July 1, 2003.

After the 2-year period expires, the retiree may continue to fill such a position only if the employer further designates the ongoing critical nature of the position in accordance with the critical labor shortage determination criteria at NRS 286.523(3).

This recommended change is consistent with the rationale for providing an exemption from PERS' reemployment restrictions for certain retirees. They are filling positions in urgent need of occupancy due to a critical labor shortage but the duration of the shortage may be for a limited time. Two years is a reasonable time frame for the employer to re-examine and re-designate the position as meeting the critical labor shortage criteria if necessary. This change is not anticipated to have any cost impact to the plan and would be incorporated into the actuary's experience study scheduled for 2004.

This BDR also contains language to provide for multiple payees under PERS' single survivor beneficiary designation. PERS' single survivor benefit was effective January 1, 2002. This benefit is designed to provide unmarried members with a survivor benefit for an individual of their choice in the event of their death before retirement. All members of the System, regardless of marital status, have been encouraged to make this designation.

Assembly Bill 431 of the 2001 legislature directed the Public Employees' Retirement Board to conduct a study of lump-sum optional retirement programs, including deferred retirement option plans more commonly referred to as DROPs and to submit a report to the Legislative Commission on or before August 1, 2002. The purpose of the study is to determine whether such programs would be beneficial for members of PERS and its participating public employers.

After careful analysis and deliberation, the Board voted to submit the study to the Legislative Commission without recommendation. Some of the areas of concern expressed by the Board were:

- Potential cost impact to the System;
- Possible reduction of retiree income replacement ratios;
- Not all members will gain financially from a lump-sum optional benefit program. There will be winners and losers; and
- Lack of consensus as to the best program to implement on behalf of PERS' members and public employers.

Next, Laura will review PERS' Investment Program.

Thank you George. Mr. Chairman, members of the committee, for the record I am Laura Wallace, Investment Officer for PERS. On page 16, we state the primary objective of PERS' investment program is to:

- *Generate an investment return sufficient to fund the pension plan over the long-term, while carefully managing risk.*

If we direct our attention to the Exhibit entitled Investment Strategy (Page 17), information concerning both market value and asset allocation for all three investment portfolios are included. The PERS' fund, currently \$12.9 billion, is invested in five asset classes. Our diversified investment strategy incorporates exposure in U.S. and international stocks, U.S. and international bonds, and U.S. real estate. The policy most reflective of our caution lies in the 45% total allocation to stocks, which is significantly less than most other large public pension funds.

The Legislators' and Judicial funds have the same primary investment objectives but a modestly different strategy incorporating three asset classes. This

approach is a function of their significantly different size. Legislators' assets, at the end of 2002, were \$3.5 million. The Judicial fund was \$4.8 million.

The next three Exhibits (pages 18, 19, & 20) include investment performance for several periods. Beginning with PERS, the cycles of the investment markets are evident in this 18-year performance history. The bottom line is that our average return through this time frame has met our actuarial return assumption of 8%.

We have included similar data for both the Legislators' and Judicial funds on the next two pages. The result is the same for the Legislators' portfolio. The Judicial fund has been managed by the Retirement System for a much shorter period of time. A time when investment returns have, on balance, been negative.

Finally, the hallmark of PERS' investment program lies in our conservative asset allocation strategy, realistic return and risk assumptions, diversification at all levels, and emphasis on compliance monitoring. Thank you. This concludes our prepared remarks. We would be pleased to answer any questions.