The Direct Approach

Legislative and Pension Overview

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Federal Legislative Update

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The State of Public Pensions

- The “Wilshire 2015 Report on State Retirement Systems: Funding Levels and Asset Allocation” found that the funded ratio for the 131 state defined benefit retirement systems covered in its study was 80 percent in 2014, up from 74 percent in 2013.

- Despite the fact that the 2008-09 market decline reduced public pension asset values by 25 percent, they were once again above their 2007 peak by 2013.

The State of Public Pensions

- This remarkable comeback has been accomplished at the same time that public plans distributed more than $1 trillion in benefits to more than eight million retirees and their survivors, and required, on a nationwide basis, only 3.9 percent of all state and local direct general spending in order to do so. (U.S. Bureau of the Census)

The State of Public Pensions

- Economic recessions of 2000-02 and 2008-09 caused required pension contributions to rise significantly at the same time that state revenues were falling, yet public plans received average of 89 percent of annual required contributions (ARCs) during the FY 2001-2013 period.
  - ✓ Only six states — NJ, PA, WA, ND, KS, CO averaged less than 75 percent.
  - ✓ Half the plans got 95 percent of their ARCs.

The State of Public Pensions

- More than one half of the 126 plans in the Public Fund Survey have reduced their investment return assumption since FY2008; the median is 7.75 percent.
- Since 2009, 36 states have increased required employee contribution rates.

The State of Public Pensions

- In July, 2015, the Pew Charitable Trusts reported that state pensions had incurred unfunded liabilities of $968 billion based on 2013 data. Scary number! But looked at another way, this shortfall is equal to approximately 0.2 percent of projected GDP over the next thirty years, the period over which the shortfall would have to be filled; alternatively, it is equal to about 2.0 percent of projected state and local tax revenues over this same period. (Dean Baker, co-founder of the Center for Economic and Policy Research)

So What's the Problem?

The Public Pension Debate

"Putting it in context"

- Who?
- What?
- Why?

Who?

- Ancient History: Grover Norquist
- Conservatives/anti-union; anti big government
- Big business – US Chamber of Commerce; Business Roundtable
- Politics: American Legislative Exchange Council (ALEC)
- Big money: Koch brothers; Laura and John Arnold

What?

- Convert Social Security to individual accounts
- Financial economics
- Switch corporate America to DC plans
- The “new” philanthropy: grants as investments; buying credibility
- Convert public sector to anything but DB plans

Why?

- Stop “corporate governance” interference
- Take power away from unions; “downsize” government
- Justify corporate America’s abandonment of DB pensions
- Divert attention from national retirement crisis
- “The only people making money off of DB plans are the participants”

So how does Washington fit into all of this?

- “Air cover” for the real action taking place at the state level
- Diversion: the problem is public pensions, not Social Security, national retirement crisis, income inequality
- Justification for changes in retirement savings incentives for budgetary reasons, not retirement policy
- Money and politics: you scratch my back, I’ll scratch yours

Danger Ahead for Public Pension Plans

- Always the danger that pension offsets will be used to "pay for" any future debt limit increase or other budget balancing efforts – BUT new two-year budget deal helps reduce this risk. Nevertheless, use of private sector pension provisions to help pay for the legislation underscores this danger.
- Tax reforms affecting retirement savings.
- "Must-do" legislation, such as tax extenders, always an invitation to mischief.

Pensions as Revenue Offsets?

- Mandatory Social Security: $81 billion over 10 years.
- Consolidate and cap tax-deferred contributions to DC plans to lower of $20,000 or 20% of income: $45.9 billion/10 years.
- Repeal Employer Pick-Up: $4.8 Billion/10 years (2005 estimate).
- Limit total amount individual can save for retirement in tax-favored settings to amount necessary to provide annual benefit of $205,000 at age 62, or about $3 million: $9 billion over 10 years.

Pensions and Tax Reform

- Suspension of inflation adjustments for the maximum benefit under DB plan, maximum combined contribution by an employer and employee to DC plan until 2024.
- Coordination of contribution limitations for 403(b) plans and governmental 457(b) plans: removes special contribution limits and simply applies section 401(k) contribution limits across the board ($17,500 plus $5,500 “catch-up for those over age 50). Total employer and employee contributions cannot exceed $52,000 for 2014.
- Application of 10-percent early distribution tax to governmental 457 plans.

Tax Reform – Is it for Real?

- Probably nothing major until after 2016 elections.
- Items on the table, scored—always a potential problem.
- Senate Finance Chair Hatch wants a pension bill, but Dems want to repeal multi-employer plan fix, while GOP wants to block DOL fiduciary rule.
- Ryan (R-WI), formerly Chair of House Ways and Means, has become new House Speaker; New House Ways and Means Chair is Brady (TX).

Possible Pension Add-on's

Public Employee Pension Transparency Act PEPTA

- ✓ No bill yet to be introduced in new Congress by Nunes (R-CA), BUT Speaker Ryan was formerly a primary sponsor, and can get it in any bill if he so desired.
- ✓ Requires sponsors to report funding info annually to Treasury using market value of liabilities (MVL), no asset smoothing.
- ✓ "Voluntary," but failure to report would lose sponsor the Federal tax-exempt treatment of muni bonds.
- ✓ Last Congress, fewer cosponsors: 10 House, 2 Senate; Brady cosponsored in 112th Congress, not in 113th Congress. No hearings last Congress.
- ✓ In 2012, attempt to use legislation fixing interest rate subsidy for Stafford loans as a vehicle for PEPTA.

Possible Pension Add-on's

Secure Annuities for Employee (SAFE) Retirement Act

- ✓ No bill yet. Previous version would create new "replacement" DB pension plan called "Annuity Accumulation Retirement Plan"; Hatch is pushing hard to find a Dem. Cosponsor.
- ✓ Permissive: State and local governments could purchase fixed annuity contracts from insurance companies for each employee. Life insurance industry would pay the pensions and bear all the investment risk.
- ✓ Hatch claims bill would eliminate pension plan underfunding prospectively, while delivering lifetime retirement income.
- ✓ Protects retirement benefits from being cut in a bankruptcy.
- ✓ Hatch says he wants to do pension bill in 2015, and vows to add his annuities proposal to any tax bill that moves.

Problems with Hatch Annuity Bill

- Existing DB plans would remain as closed plans, so costs would increase; doesn't address existing UAAL.
- Unsure level of income replacement; no requirement that once begun, annual purchase of annuities must continue or be consistent.
- State insurance guaranty programs vary widely; are NOT pre-funded.
- No survivor and disability benefits.
- Once one state decides to try it, others are likely to follow.

Government Pension Offset (GPO) – Windfall Elimination Provision (WEP) *Reform?*

- Brady (R-TX), Neal (D-MA) reform bill (H.R. 711): replace WEP with new formula; could increase SS benefits from $1,000/yr. on average up to $1,600/yr. for future retirees. Revenue neutral due to enhanced enforcement thanks to 30 years income history from Medicare contrib. data) and more who would be subject to WEP.
- "Winners and losers" -- workers who are currently impacted by WEP and have reported non-SS pensions will win; workers with 30 to 35 yrs of SS earnings lose current exemption, and will lose.
- 10/1/2015: SS Advisory Board recommended repeal and replacement of current formula with "proportional formula" and refer to Brady/Neal bill as example of such,
- Brady as Chair of W&M is BIG help!

GPO-WEP

Repeal?

- Davis (R-IL), Schiff (D-CA) GPO/WEP repeal bill (H.R. 973) has 122 cosponsors (10/16); a Senate companion introduced by Brown (D-OH) has 18 cosponsors. Support for total repeal seems to be waning: similar repeal legislation in the 111th Congress (2009-2010), had 334 cosponsors in the House; in the 112th Congress (2011-2012), House cosponsors dropped to 170; and in the last Congress, House cosponsors fell to 133.
- Primary problem continues to be cost of repeal, which could be about $90 billion combined.
- Potential linkage of GPO/WEP repeal to mandatory SS
- “Dual entitlement” rule in private sector: beneficiary receives higher of his/her SS or of spouse/widow(er)’s benefit, but not both; repeal would cost $500 billion over a five-year period (2003 est.)

New Legislative Issue

Dold Amendment to Elementary and Secondary Education Act (ESEA)

- Amends H.R. 5 to prohibit states from requiring LEA's to use federal education funds to pay for more than normal cost of Title 1 Teacher pension; not in Senate version
- TN letter to Sen. Alexander (R-TN), Cong. Roe (R-TN)
- Could extend to other Federally-funded positions such as "Staffing for Adequate Fire and Emergency Response" (SAFER) Grants and "Community Oriented Policing Services" (COPS) program.
- In House/Senate Conference

2014 Regulatory Issues

Treasury: Normal Retirement Age Regulations

- ✓ Released in final form in 2007, but application to governmental plans extended several times.
- ✓ Problems with use of service in defining the time when employee was eligible for unreduced benefit.
- ✓ Safe harbors in regs were unworkable for public plans.
- ✓ 2012 notice of intent to amend regs for public plans, with focus on in-service distributions before age 62.
- ✓ What about return-to-work? Part time work? DROPS?
- ✓ Devil will be in the detail of the new regulations.

Treasury: Definition of Governmental Plan

- ✓ BIG DEAL! Governmental plans exempt from reporting, participation, vesting, and fiduciary standards of ERISA.
- ✓ ANPRM issued 11/8/2011; no actual proposed regs yet, but new charter school regs -- back on the front burner?
- ✓ 5 “main” factors (Control of Governing Body; Public Election of Governing Body; Fiscal Responsibility; Treatment of Employees as Public Employees; Delegated Sovereign Powers.
- ✓ Eight “other” factors: Operational Control; Direct Funding; Specific Enabling Law; Treatment as Govt Entity for Fed Tax Purposes; Treatment Under State Law; Court Decisions; No Private Interest; Serves a Governmental Purpose.

Treasury: Individual Elections/Pick-Up Rule

- ✓ Orange Co., San Jose: individual elections into new tiers.
- ✓ Rev. Rul. 2006-42: Cash-or-deferred elections?
- ✓ Problems: impact on purchase of service credits; chill on reform flexibility; “cookie cutter” PLR.
- ✓ 8/7/15 – PLR says individual member elections into differing benefit tiers with varying contribution levels is impermissible cash or deferred arrangement.
- ✓ Sanchez (D-CA) would permit employer contributions as picked up even if the employee can make irrevocable election between two alternative benefit formulas involving the same or different levels of employee $$.

Medicare Part B Premium Hike

- ✓ No SS COLA means that 70% of Medicare Part B beneficiaries receiving SS benefits are "held harmless" from having to pay any Part B Medicare premium increase, but everyone else, including public employees outside SS, has to pay ALL of Part B increase.
- ✓ In 2016, Part B standard premium would have increased about 50%; instead of going from $104 monthly to $120, would have jumped to $159 for most recipients -- largest increase in the history of Medicare.
- ✓ NCTR, NASRA, NCPERS, NEA and AFT demand action.
- ✓ "Fix" in new two-year budget deal: Treasury loans money to Medicare; those not covered by "hold-harmless" still pay more, but premium only jumps to $120/mo., plus $3/mo. surcharge until "loan" repaid. Everyone else still off the hook!

Questions?

The Direct Approach

State Legislative Update

Dan Wattles,
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State Legislative Update

84th Session Rewind

- Changing of the Guard
- Session Expectations
- Session Results

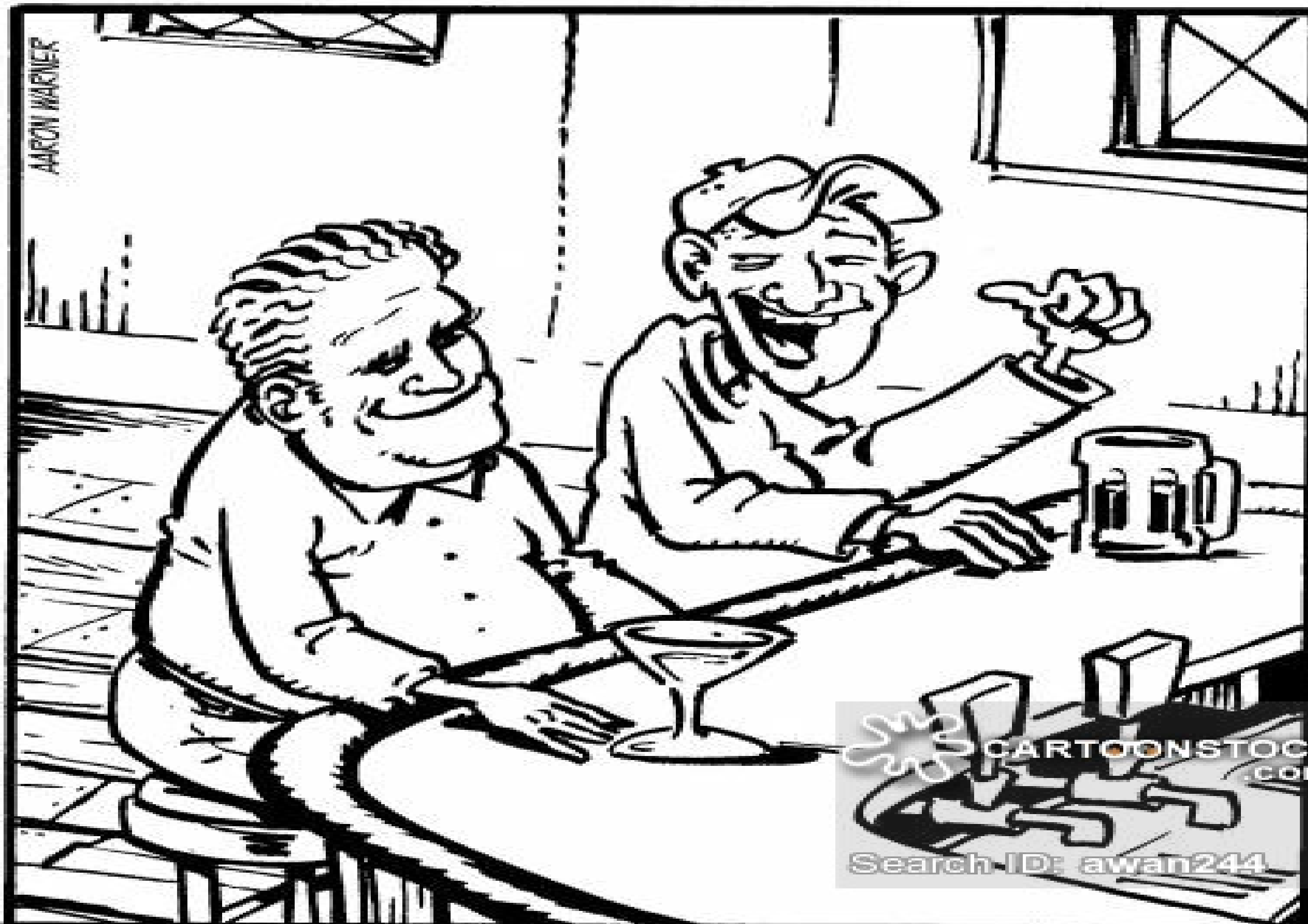
The Interim Period

- More Legislative Changes ahead
- House & Senate Interim Charges

TMRS Activities

- TMRS Strategic Plan
- Review Role of Advisory Committee
- Framework for Legislative Changes
- Benefits of Using TMRS' Review Structure

Takeaways



"A 401K? ARE YOU KIDDING? I CAN'T EVEN RUN A 5K!"

84th Session Rewind

84th Session Rewind: Changing of the Guard

- New Governor, Lt. Governor, Comptroller, Attorney General, and Commissioners of Agriculture and General Land Office
- 9 new Senators; 5 additional Senators with two sessions of experience
- New Chair of Senate State Affairs Committee; 4 other new State Affairs Committee members
- 28 new House members; 40 in second term
- New Chair of House Pensions Committee for 3rd consecutive session
- 6 (of 7) new Pensions Committee members

84th Session Rewind: Pre-session Expectations

- Continued anti-pension fervor
- Pension systems in other states continually in news
- Certain Texas plans garnered attention
- Expectations were for some degree of pension focus
- Difficult issues; member experience with pension issues

84th Session Rewind: Session Results

84th & 83Rd Regular Legislative Sessions Final Statistics (as of June 1, 2015)								
	House				Senate			
	84R	83R	Diff	%	84R	83R	Diff	%
Bills Filed	4,207	3,950	+257	+6%	2,069	1,918	+151	+8%
Bills Passed	818	732	+86	+12%	504	705	-201	- 29%
Joint Resolutions Filed	133	130	+3	+2%	67	63	+4	+1%
Joint Resolutions Passed	2	6	- 4	-67%	5	4	+1	+25%
Total Bills Filed	6,276	5,868	408	+7%				
Total Bills Passed	1,322	1,437	- 115	- 8%				
% Bills Passed	21%	24%						

84th Session Rewind: Session Results

No TMRS-specific bills sponsored or endorsed by TMRS Board

However, 4 bills filed by legislators on behalf of individual constituents:

- HB 2188 (Lozano) – Return to Work
- HB 3100 (Lozano) – Return to Work
- HB 4080 (Smithee) – Fixed rate COLA
- SB 1381 (Estes) – Fixed rate COLA
- None of the four bills passed

84th Session Rewind: Session Results

Positive Results for Pension Systems

- HB 9 (Flynn) – Employees Retirement System
- HB 1 (Otto) – Appropriations Act
- SB 463 (Huffman) – TCDRS Fund Restructuring
- HB 3310 (Paul) – Local Pension Bill

The Interim Period

The Interim Period: More Changes Ahead

Since the end of the 84th Session, more legislative turnover (announcements)

- 2 State Senators not running for re-election
  - Senators Eltife and Fraser
- 14 State Representatives not running for re-election or running for other office
  - Includes 6 committee chairmen, including chair and vice chair of Appropriations Committee: Representatives Otto and Turner

The Interim Period: Interim Charges

Senate and House Interim Committee Charges

- Interim committee charges are made by Lt. Governor (Senate) and Speaker (House) to study policy issues leading to the next session
- Following each legislative session, members are asked by Lt. Governor and Speaker to recommend study topics for interim period
- Committee charges are typically announced in latter part of year
- Hearings are held across state to gather input
- Committees report back prior to session

The Interim Period: Interim Charges

Senate and House Interim Charges

- Lt. Governor has announced appointments to two joint-study committees and to the HHS Transition Legislative Oversight Committee
- Also announced interim charges for all Senate standing committees in mid-October
- Speaker released interim charges for the House standing committees in early November

The Interim Period: Interim Charges

Senate State Affairs Committee Charges

- No “specific” pension issue charge
- General monitoring charge: “Monitor changes made to Employees Retirement System regarding member contributions and proposed reforms to the Teacher Retirement System”
- Union dues charge: “Examine the practice of using public funds and employees for the payment processing of union dues. Make recommendations on whether Texas should end this practice”

The Interim Period: Interim Charges

Senate Finance Committee Charges

- Fiscal Responsibility Charge: “Review and make recommendations to reduce state debt liabilities, including state pension liability”
- *Property Tax Process Charge: “Study the property tax process, including the appraisal system, and recommend ways to promote transparency, simplicity, and accountability by all taxing entities”
- *Reduce Tax Burden Charge: “Examine and develop and further reduce the tax burden on property owners”
- General Monitoring Charge: “Monitor legislation passed by the 84th Legislature and make recommendations for any legislation needed to improve, enhance, and/or complete tax relief provided to property owners”

*Charges given to a select subcommittee on Property Tax Reform and Relief

The Interim Period: Interim Charges

House Pensions Committee Charges *(6 total; paraphrased)*

- Analyze assumed rates of return, asset class structures, investment goals and make recommendations to ensure the investment structure of public pension funds are meeting fiduciary responsibilities
- Evaluate performance benchmarks and the impact portfolio diversification and market assumptions have on achieving investment returns; Analyze the fee structure and investment strategy for various investment classes to ensure costs are reasonable and competitive
- Examine fiscal and policy impacts on structural reforms that would increase pension plans' actuarial soundness and the feasibility of using one-time funding to reduce unfunded liabilities
- Examine compliance with GASB 67 & 68 and identify their effect on the state's pension systems

The Interim Period: Interim Charges

Other House Committee Charges

- Appropriations Committee: "Monitor the implementation of HB 9 and study projections toward actuarial soundness of the Employee Retirement System. Examine issues and costs associated with granting COLAs or "13th Checks" to retired state employees and teachers"
- Federal and State Powers Committee: "Examine the status of Texas statutes prohibiting or restricting investment in foreign nations. Determine whether and to what extent Texas has the authority to continue or renew its own economic sanctions in light of recent and potential future actions by the federal government"

TMRS Activities

TMRS Activities: TMRS Strategic Plan

- TMRS Board discussed possible changes to five-year strategic plan at August Board meeting
- Draft plan would cover years 2016-2020
- Would include a total of five goals
- Two of the five goals are new and relate to the Board's governance structure and providing a framework for possible legislative changes

TMRS Activities: Advisory Committee Review

Proposed Goal 3 (new language):
"Identify the Best Governance Structure and establish a prudent policy framework for TMRS"

- Proposed Objective 3 of this goal is "Revisit and optimize the role of the Advisory Committee on Retirement Matters"

TMRS Activities: Framework for Legislative Changes

Proposed Goal 5 (New): “Pursue a legislative agenda that supports the TMRS mission and vision.” Four objectives being considered to meet this goal:

- Evaluate “Return to Work” provisions
- Create a plan for determining under what future circumstances TMRS would consider implementing “gain sharing”
- Identify legislative issues previously studied by the Advisory Committee where consensus was not reached (COLA; eligibility threshold)
- Develop and promote a legislative bill to clarify aspects of the TMRS Act

TMRS Activities: Benefits of TMRS Structure

Benefits of using TMRS planning structure to propose design changes:

- Helps identify and limit unintended consequences – issues that are inherent in a complex plan
- TMRS staff and consultants are available to analyze and uncover potential unintended consequences
- Ensures proposals are thoroughly studied and comply with federal law and regulations
- Helps increase support among constituencies using successful Advisory Committee structure
- Increases communication among cities, members, and retirees

Takeaways

Takeaways

- We operate in a dynamic environment
- There will continue to be change at the legislature
- The Legislature is interested in the success of public pensions
- TMRS will continue to review and propose system improvements


I'VE GOT A STOCK HERE THAT COULD REALLY EXCEL
REALLY EXCEL?
EXCEL?
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THIS IS MADNESS! I CAN'T TAKE ANYMORE
GOOD BYE!
GOOD BYE?
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BUY!
I'VE GOT A STOCK HERE

QUESTIONS?