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Senate State and Local Government Committee

Testimony on HB 1040

Presented by Gordy Smith

Madam Chair and members of the Senate State and Local Government Committee, my name is Gordy Smith and it is my privilege to appear before you today in opposition to HB1040. I worked for the State Auditor's Office for over 36 years before retiring because of health issues in 2013. I believe this bill will be detrimental to the hiring and retaining of future state employees. In addition, I believe it will also cause current and retired state employees genuine concern as to whether the state will live up to its responsibility to pay their full retirement benefits as promised when they were initially hired.

Two of the primary reasons that state employees remain employed with the state are the defined benefit retirement program and the excellent health care benefits. Terminating the defined benefit retirement plan removes one of these incentives. We have already heard the Governor and some legislators speak about spending tens of millions of dollars on workforce recruitment and retention in the upcoming biennium. Does this effort exclude state employees? Removing half their incentive to remain employed with the state certainly appears as though it does. Spending millions of dollars to help private employers retain their employees while passing legislation which damages the state's ability to hire and retain its employees makes absolutely no sense.

Switching the plan to a defined contribution plan is going to cost significantly more money over the next 20 years than fixing the plan according to actuarial calculations (billions of dollars by one actuarial estimate). Why not invest the money to fix the plan and keep one of the best aspects of employment with the state of North Dakota? State employees overwhelmingly prefer the defined benefit retirement program (as survey results show) so it seems ludicrous that legislators are going to turn around and spend billions of dollars over the next 20 years to close the defined benefit plan and give state employees something they don't want.

Most other states provide a defined benefit plan and some of those that previously switched to a defined contribution plan have either switched back or are considering it.

Media reports cite that the turnover rate for state employees last year was 14% which was the highest ever I believe. Salary studies have consistently shown that state employees are generally paid less than their private sector counterparts. These salary studies include comparisons of fringe benefits and the state's defined benefit retirement plan generally is used to offset a portion of the difference in salaries. Closing of that plan will only increase the difference and logically will result in more turnover. Those of you who are business owners or management understand the true cost of turnover.

The defined benefit plan provides the state employees a significantly better retirement benefit. Based on certain assumptions (i.e. annual rate of return), for an employee with 21 years of service who averaged \$40,000 of annual salary, the defined benefit plan would provide almost double the annual retirement benefit. If the state is going to remove this substantial safety net, I believe substantially higher salaries are going to be needed in order to retain staff at the levels that are currently retained. This is especially true for the professional classifications such as lawyers, accountants, architects and engineers.

There are many other ways that the switch to a defined contribution plan is disadvantageous to state employees. For example, in the defined benefit plan their investments are pooled and the investment risks are shared by the entire pool vs the individual investor having the risk of the investments under a defined contribution plan. In the defined benefit plan experts make the investment management decisions while the individuals make those decisions in the defined contribution plan. In addition, as shown earlier the employee can estimate their future income in the defined benefit plan while in the defined contribution plan future income is uncertain.

I really think it's important that the full Legislature consider the issue of fairness when they vote on HB1040. The Teachers Fund For Retirement (TFFR) is a defined benefit retirement plan and its latest audit showed it had an unfunded liability of approximately \$1 billion. Yet that fund is not included in this legislation. Instead that fund was given the chance to take less stringent measures to put it on the road to recovery over the next 20-

25 years. A cynical person might speculate that politics played a part in the decision to permit that fund to adopt measures to allow it to recover. Meanwhile the "nuclear option" was used on the PERS fund. The cynical person might speculate that the TFFR fund has members scattered throughout the state and the idea of terminating that defined benefit fund would cause an uproar and all legislators would hear about it. Meanwhile the majority of the PERS membership resides in the Bismarck-Mandan area and thus only a limited number of legislators will hear the complaints. Is this really fair? Why should politics play any part in such a large decision affecting so many loyal state employees?

Is it fair the Governor and this Legislature spend tens of millions of dollars to improve the hiring and retention of employees for the private sector while spending billions of dollars over the next 20 years to decrease the hiring and retention of state employees? Does that even make sense?

Please keep in mind that for the past several years legislators were asked to address the unfunded liability of the PERS defined benefit plan and they declined to do so. It appears that the sponsors of HB1040 just want to kill the PERS defined retirement plan regardless of fairness (compared to TFFR), despite the fact that the Legislature was asked to fix it for years and declined, not caring what the members of the plan prefer and without serious consideration to the fact it is going to cost several times more to kill it than to fix it. In this case "the end justifies the means" no matter how ludicrous it seems.

Current and retired employees have genuine and understandable concerns about receiving their full and promised retirement benefits if the defined benefit plan is terminated. While this Legislature can pass a law requiring future contributions from Legacy Fund earnings or any other funding source, future legislatures can just as easily repeal that section of the law. This Legislature cannot absolutely bind future legislatures to supporting the full payment of the commitments made to the current and retired state employees. While there is a moral and almost certainly a legal obligation to pay those commitments, that does not lessen the concerns that loyal employees who admirably have served the state have regarding their retirement payments.

SB2239 which was passed by the Senate appears to me to be a common-sense fix for the PERS defined benefit plan. It provides a path to make the plan financially sound over a reasonable period of time. It also provides any employee the option of participating in a defined contribution plan should they wish (although traditionally a significant majority of state employees have not chosen that alternative).

In summary, I believe this bill will result in spending billions of additional dollars over the next 20 years to close the plan than would be necessary to fix it and will result in the state having a retirement plan that a significant majority of state employees do not want. It will also ultimately result in damaging the hiring and retention of state employees. Furthermore, passage of this bill will only cause current and retired state employees serious and understandable concern as to the state's intention of honoring their responsibility to pay them their full retirement that they earned and were promised when they were hired. It is simply the worst solution to addressing the unfunded liability the PERS defined benefit fund faces.

I respectfully request that you give HB1040 a do not pass recommendation. Thank you for your time and I would do my best to answer any questions the committee may have.