PENSION MANAGEMENT OVERSIGHT COMMISSION

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MEETING MINUTES[1]

Meeting Date: October 13, 1999
Meeting Time: 10:00 A.M.
Meeting Place: State House, 200 W. Washington St., Room 431
Meeting City: Indianapolis, Indiana
Meeting Number: 2

Members Present: **Sen. Joseph Harrison, Chair; Sen. Allie Craycraft; Sen. Larry Lutz; Rep. Thomas Kromkowski; Rep. Ron Liggett; Rep. Lawrence Buell; Steve Meno; William Gettings, Jr; Connie Lux;**

Members Absent: **Sen. Thomas Weatherwax; Rep. Richard Mangus; Claude Davis.**

1. PERF/TRF Legislation Preliminary Draft 3329

The Chair of the Pension Management Oversight Commission (PMOC), Sen. Harrison, called the second meeting to order at 10:11 A.M. Sen. Harrison introduced the PMOC members and the staff. Sen. Harrison then recognized Ms. Mary Beth Braitman of the law firm of Ice Miller Donadio & Ryan, outside counsel for the Public Employees Retirement Fund (PERF) and the Teachers' Retirement Fund (TRF). Ms. Braitman distributed a section by section analysis of PD 3329. Ms. Braitman told the PMOC that PD 3329 would establish both PERF and TRF as independent bodies corporate and politic, and not departments or agencies of the State of Indiana. Ms. Braitman also distributed copies of Separate Body Corporate and Politic "Comparables" for Indiana and copies of Separate Body Corporate and Politic "Comparables" for other midwest pension systems.

Ms. Braitman told the PMOC that Section 1 eliminated PERF and TRF staff as part of the state employee personnel administration. The PERF and TRF Boards of Trustees will have the responsibility to determine staffing. Continuing, Ms. Braitman said that Section 2 of the bill establishes PERF and TRF each as a body corporate and politic, an independent instrumentality exercising essential government functions. It also clarifies that PERF and TRF

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boards, employees, and funds remain in the same status as they currently are for purposes of contract claims, tort claims, and civil rights claims.

Section 3, Ms. Braitman said, deletes biennial appropriation language for expenses as well as language that offsets appropriation by fund earnings. Deletion of this language will result in the funds paying their own administrative expenses, as they currently do pursuant to the offset language. It leaves the liability for funding liabilities exactly as it currently is in statutes.

Ms. Braitman said that Section 4 retains current law as it relates to the PERF Board being primary fiduciary of PERF and being subject to the prudent expert rule. This section, Ms. Braitman said, amends the PERF Board of Trustees' duties to include additional employment, budgeting, funding, and reporting responsibilities. Ms. Bratiman added that this is consistent with the Uniform Management of Public Employee Retirement Systems Act, as approved and recommended for enactment in all states by the National Conference of Commissioners on Uniform State Laws. These additional duties are also consistent with other Indiana corporate bodies and other Midwest public pension systems.

Section 5, explained Ms. Braitman, contains a corresponding enlargement of PERF Board powers to conduct its business as fiduciaries of the Fund.

Ms. Braitman said that Section 6 retains current law as it relates to the TRF Board being primary fiduciary of TRF, and being subject to the prudent expert rule. This section, Ms. Braitman said, amends the TRF Board of Trustees' duties to include additional employment, budgeting, funding, and reporting responsibilities. Ms. Bratiman added that this is consistent with the Uniform Management of Public Employee Retirement Systems Act. These additional duties are also consistent with other Indiana corporate bodies and other Midwest public pension systems.

Ms. Braitman stated that Section 7 contains a corresponding enlargement of TRF Board powers to conduct its business as fiduciaries of the Fund.

Section 8 conforms the 1977 Police & Firefighters Advisory Committee provisions to be consistent with the other changes described above. It makes their expenses subject to the PERF Board approval. It also clarifies that the Committee can include active or retired members.

Sen. Harrison next recognized Mr. E. William Butler, Director of PERF. In his prepared remarks, Mr. Butler told the PMOC that he has been Director of PERF since November, 1998. Mr. Butler told the PMOC that he has day to day responsibility for the safe and proper administration of a $10 billion trust fund that is charged with safeguarding the retirement expectations of more than one quarter of a million current and retired public employees in this state. Mr. Butler said that the ultimate responsibility for the fund rests on the shoulders of five Trustees who are the principal fiduciaries of this trust. He noted that PERF ranks in the top 100 pension funds in this country, making it one of the largest in the world.

Continuing, Mr. Butler said that PERF finds itself competing in two markets. The first is the market that serves the retirement needs of the public employees in this state. The second market is the global market composed of large institutional investors, each of whom is competing for the best return on its investment dollars. Mr. Butler said that the business of PERF and TRF is defined by these two markets functions; the prudent and effective investment of assets and the timely and efficient delivery of benefits and services to members.

In commenting further, Mr. Butler said that over the last decade, the General Assembly has given recognition to the unique nature of the pension funds through passage of legislation that has modernized and strengthened them. He cited such measure as the adoption of the "Prudent Expert" standard, changes in the funding provisions for the police and firefighter pension funds and giving members more of a voice in the investment of their Annuity Savings Accounts. Mr. Butler stated that the progress represented by these measures is most clearly seen in the passage of the constitutional referendum in 1996 that allowed the funds to invest in the equity market.

Mr. Butler went on to say that the funds are not simply expected to invest wisely, but that they are compelled to be competitive in a very sophisticated and complex global market. The pace and demands of these markets require investors such as PERF and TRF to be nimble and responsive. Mr. Butler also said that while the funds have had to expand their investment programs significantly to meet new obligations, establishing the funds as separate bodies corporate and politic would give them the tools they need to carry them out.

Mr. Butler said that along with the investment program, it is important to deliver benefits and services to members. He said that the Trustees of PERF have given him the task of bringing services levels up to the point where PERF meets or, exceeds the requirements set out by statute. Mr. Butler further commented that the PERF Board of Trustees has given great consideration to the concept in the legislation that PMOC is considering. He said that the Board enthusiastically supports this legislation, not only as the most efficient and effective way to meet its fiduciary obligations, but also as a final piece in the overall effort of the legislature to modernize the funds.

He continued that this legislation would put the funds on a sound business-like basis and allow them to function competitively in a highly complex atmosphere. Mr. Butler continued that while the funds would remain part of the overall government structure, this legislation would put them on equal footing with other large pension funds and institutional investors. Mr. Butler observed that this legislation would give full recognition to the concept that the trustees, in their roles as fiduciaries, bear the ultimate responsibility for carrying out the statutory requirements as laid down by the General Assembly.

In commenting about reporting requirements, Mr. Butler observed that the PERF Board of Trustees proposes to create a fuller and more informative reporting process to the legislature that would not only give better information about how the funds conduct their business but would also put the legislature in a better position to consider legislative proposals for the public retirement programs in Indiana.

Mr. Butler went on to say that as fiduciaries of the trusts, the trustees are required by law to exercise independent and exclusive authority over the investment and management of those assets. He reminded the PMOC that the trusts hold no state money; rather the assets are held in trust for the benefit of the members. Mr. Butler told the PMOC that it is to those members that the trustees owe their fiduciary duty.

In closing, Mr. Butler said that there is no cost to the State of Indiana under this proposal. He observed that by statute, the funds take their operating expense from their investment earnings and that this proposal would have no impact on the revenues of the state.

In response to a question, Mr. Butler said that the amount of control of the Governor and the General Assembly would remain roughly the same as is now the case. In response to another PMOC question about private pension funds and public pension funds, Mr. Butler said that private pension funds are subject to ERISA and public pension funds are not.

The Chair next called upon Mr. William Christopher, Director of TRF. Mr Christopher said that he just returned from a meeting with directors of teachers funds from around the nation and that he learned these funds are attempting to concentrate more on services to its members. He said that this legislation would allow that very thing. Mr. Christopher told the PMOC that TRF and PERF are working closely to maximize costs savings and enhance mutual work. He cited a joint staff technology project as an example of this. He further observed that because of the complexities of the duties of public retirement funds, there is a need to modernize the tools that the board members use to administer these funds.

Sen. Harrison called upon Mr. Fred Armstrong, Mayor of Columbus. Mr. Armstrong told the PMOC that he serves on the Indiana Association of Cities and Towns' (IACT) legislative Committee and Labor Task Force. He related that he also serves on the 1977 Police and Firefighters Pension Fund Advisory Committee and has done so since July 1, 1996. He said that he was chosen to represent IACT to offer remarks on PERF and its impact on all municipalities. Mayor Armstrong stated that IACT appreciates PERF's effort in taking the lead to structure PERF in a way which would allow improvements in member services and communications. He went on to say that PERF is an important employment benefit that municipalities can offer its workers. Mayor Armstrong also that in August, 1999, IACT sought comments from its Legislative Executive Committee, the members who are in a leadership position, concerning the initiative to allow PERF to become a separate body, corporate and politic. He reported that there were no negative responses to this initiative. Mr. Armstrong also said that there were no concerns voiced at the recently concluded IACT annual conference.

Mayor Armstrong went on to say the IACT members have hundreds of workers who are members of PERF. He said that anytime municipalities and their employees are better able to communicate with the PERF staff, the easier it is for all to perform their duties. The more information that municipalities and their workers receive on their pension benefits, the greater the understanding of their options and the value of a pension system. Mayor Armstrong told the PMOC that the IACT pledges to support the process of increased pension information and services. He said that IACT's monthly publication "Actionlines" will be running an article in its upcoming issue on PERF's CLARETY computer system. Mayor Armstrong asserted that IACT is supportive of PERF becoming a separate body, corporate and politic to continue its modernization process. In addition, he stated that it would be IACT's goal to see the 1977 Advisory Committee continue in its present service as a "watch dog" and go-between for PERF participants and PERF.

Sen. Harrision called upon Mr. Mark Webb, Chief Legal Counsel for PERF. Mr. Webb said that PERF favors the proposal. Mr. Tom Miller, President of the Professional Firefighters Union of Indiana was next recognized by the Chair. Mr. Miller told the PMOC that as President of the Union and as Chair of the 1977 Police and Fire Pension Fund Advisory Committee he supports the legislation. Mr. Steve Moberly, Executive Director of the Indiana Retired Teachers Association (IRTA) was then called upon by Sen. Harrison. Mr. Moberly introduced Mr. Bob White, President of the IRTA. Mr. Moberly then told the PMOC that the IRTA supports the concept and that the legislation will give TRF the tools it needs to better serve its members. Mr. Bill Murphy, Director of the Indiana Retired Public Employees Association (IRPEA), told the PMOC that IRPEA supports the proposal. Mr. Leo Blackwell of the Fraternal Order of Police (FOP), told the PMOC that the FOP supports the proposal. Both Mr. Miller and Mr. Blackwell told the PMOC that this legislation will allow PERF to enhance services to its members. Mr. Don Hogan of the Indiana Teachers Association (ISTA) told the PMOC that ISTA supports the proposal.

The Chair called for disposition of PD 3329. Sen. Craycraft moved and Rep. Kromkowski seconded the motion to recommend introduction of PD 3329. The Chair called for a roll call vote and PD 3329 passed nine to zero.

2. Taxation of Survivor and Disability Benefits for Police and Firefighters PD 3445

Sen. Harrison called upon Ms. Bratiman to discuss and present this issue. PD 3445 was distributed to the PMOC members. Ms. Braitman told the PMOC that PD 3445 deals with survivor and disability benefits for police and firefighters. The bill separates the provisions concerning survivor benefits for police officers and firefighters into separate sections based on whether the death was in the line of duty or not in the line of duty. It makes the definition of "dies in the line of duty" used in the survivors benefits statutes uniform for all police officers and uniform for all firefighters. She went on to say that the bill separates the provisions concerning the 1977 Fund disability benefits for covered impairments into separate provisions based on the class of impairment.

Ms. Braitman told the PMOC that this legislation would allow members and survivors to receive certain line of duty death and disability and survivor benefits without paying federal tax on those benefits. Ms. Braitman explained to the PMOC that the police and firefighters submitted a request for a private letter ruling to the Internal Revenue Service (IRS) regarding this issue. Ms. Braitman informed the PMOC that the private letter ruling from the IRS has been received. She said that the IRS suggested that if certain structural, not substantive, changes were made to the police and firefighter funds, the IRS would rule death and disability benefits to be non-taxable. The ruling laid out what currently is taxable and what is non-taxable and the direction that the General Assembly should take in order to make additional benefits non-taxable.

The Chair recognized Mr. Leo Blackwell of the FOP. Mr. Blackwell told the PMOC that the FOP supports the concept of PD 3445. Mr. Tom Miller of the Professional Firefighters Union of Indiana said that taxation issues are complex and represent problems for his members. He also said that he supports PD 3445. In response to a question from the Chair regarding the possibility that the Indiana General Assembly would be an arbiter for disability benefits, Ms. Braitman said that it remains an issue. Ms. Braitman said that with PD 3445 the initial determination would be made by the local board and reviewed by the review board of the 1977 Police and Firefighter Pension Fund Advisory Committee as a central, neutral body.

The Chair called for disposition of PD 3445. Rep Liggett moved and Sen. Craycraft seconded the motion. The Chair called for a roll call vote, and PD 3445 was recommended for introduction by a vote of nine to zero.

3. <u>Judges' Retirement System-Judge Mary Lee Comer</u>

Sen. Harrison next called upon Judge Mary Lee Comer of Hendricks County. Judge Comer said that she was representing the Indiana Judges' Association (IJA). She stated that the IJA is requesting the PMOC consider the following issues:

<u>A) Cost of Living Adjustment (COLA) for the 1985 Pension Plan</u>. Judge Comer informed the PMOC that the pension benefit for judges in the 1985 Judges' Pension Plan is fixed as of the date of retirement. This request, she said, would grant to the judges in this plan the same COLA that is granted to PERF and TRF recipients by the General Assembly. Judge Comer went on to say that 29 states provide COLAs for their retired judges. Commenting further, Judge Comer reported that, although Indiana is ranked fourteenth nationally in population, the annual pension benefit received by its judges is ranked thirty second nationally.

<u>B) Add Magistrates to the 1985 Judges Plan</u>. Judge Comer told the PMOC that Indiana's magistrates are to judges what chief deputy prosecutors are to prosecutors. They are a critical part of the function of the office. She said that chief deputy prosecutors are included in the Prosecuting Attorneys Retirement Fund. This request, she continued, recognizes the similar positions and seeks parity for magistrates.

Judge Comer noted that this request had been brought before the PMOC during the 1999 interim, and both were approved by the Commission. In the handout provided by Judge Comer, the cost for Proposal A, COLA for members of the 1985 Plan, was estimated at approximately $604,000 over the next five years, or an average of about $121,000 per year.

The cost for Proposal B, adding full-time magistrates to the Judges' Retirement System, would be approximately $126,000 over the next five years.

Sen. Harrison asked Judge Comer about newspaper reports noting judges asking for a salary increase. Judge Comer told Sen. Harrison and the PMOC that the Judges were planning to request a salary increase through the Commission on Courts. Judge Comer reported that the Judges have not had a salary increase since 1995, and that this is hurting the morale of the judges. Rep. Kromkowski commented that he carried the COLA bill last session, but there were problems with the magistrate issue. In response to a member comment, Sen. Harrison said that the 1977 Judges Plan allows benefits based on the salary of a sitting judge, while the 1985 Judges' Plan is tied to the salary of the judge at the time of retirement.

Sen. Harrison said the Commission would discuss these issues, either separately or together at the PMOC's final meeting.

4. Prosecuting Attorneys Retirement Fund (PARF) Issues - Deborah Daniels

Sen. Harrison next recognized Ms. Deborah Daniels, representing the Association of Indiana Prosecuting Attorneys. Ms. Daniels briefly described a number of issues concerning PARF. Ms. Daniels then introduced Mr. John A. Larson, Warren County Prosecuting Attorney. Mr. Larson distributed copies of his prepared remarks to the PMOC. In his presentation, Mr. Larson told the Commission that PARF was established in 1989 by the General Assembly, and that it is administered by PERF. Mr. Larson said that PARF provides retirement and disability benefits for elected prosecutors and their chief deputies, as well as a few other individuals (a total of approximately 182 people throughout the State).

Mr. Larson told the Commission that the Prosecuting Attorneys are asking for the following changes to the current PARF plan.

1) Pro rate benefits for partial years of service.
2) Eliminate the requirement that Prosecuting Attorneys continue to contribute after 22 years of service. Mr. Larson said that these two provisions would provide parity with the Judges' Retirement System.
3) Change the benefit multiplier for disability benefits to the same multiplier as in the Judges' Plan.
4) Change the eligibility for disability benefits to disability rendering the member unable to perform the duties of the prosecutor.
5) Eliminate the requirement that a member have at least five years of service in order to be eligible for disability benefits.
6) Change the requirement for vesting from ten years to eight years.
7) Benefit multiplier changed such that benefit would be now 60% of salary after 22 years of service where previously it was 50% of salary after 20 years of service.
8) Salary definition changed from salary paid at time of separation from service to annual salary being paid for the office the participant held at separation of service.

Ms. Daniels distributed a fiscal impact statement from Mr. Doug Todd of McCready & Keene, actuaries for the PARF. Mr. Larson reported that this proposal would increase annual funding for the PARF by $754,000. Sen. Harrision asked both Ms. Daniels and Mr. Larson if any thought had been given to which of the items are a priority. Ms. Daniels remarked that a provision requesting a COLA had been dropped from HB 2052, from the 1999 session.

5. Other Business

Sen. Harrison brought up the issue of taxation of federal retiree benefits. He told the Commission that much testimony had been received on this issue. Sen. Harrison then read the following statement regarding the issue of taxation of federal retiree benefits.

> The issue of taxation of federal retiree benefits was brought before the Pension Management Oversight Commission. The Commission heard testimony on the subject from interested parties. In addition, the Commission received information on how other states treat federal retirement benefits. The Commission also heard testimony that some states tax state and federal retirement benefits in the same manner, although some states do not. The Commission recommends that whatever is done regarding the taxation of retirement benefits must be done with equity for both state and federal retirees. In addition, it should be noted that this issue is more of a tax issue than a pension issue, and therefore any final recommendations should be made only after the issue has been reviewed by the Commission on State Taxation and Finance Policy.

By consent, the Commission agreed to pass this on the Commission on State Tax and Financing Policy.

Sen. Harrison announced that the next meeting of the PMOC would be the final meeting. He set the next meeting for October 28, 1999, at 10:00 a.m. The agenda for the final meeting will consist of the following:

1) Final Report
2) Judges Issues
3) PARF Issues
4) Taxation of federal retiree benefits
5) Police and Fire Survivor and Disability Issues

With no further business, the Chair adjourned the meeting at 11:30 a.m.