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Federal Retirement Policy Report for CalPERS Board
May 2017

I. Developments in Protecting Public Sector Defined Benefit Plans

CalPERS' 2017 Federal Retirement Security Priorities advocate for the preservation of defined benefit retirement plans and against federal incentives or options to replace defined benefit pension plans and federal intervention in state and local pension plans.

1. New Developments Since Last Report:

- **Public Pension Report –** The Center for State and Local Government Excellence and the National Association of State Retirement Administrators released a new report titled, Public Pension Reporting and Disclosure: The Current State of Practice and Examples of What Works Well . The report used data from 83 of the largest statewide pension plans, as well as five case studies, to address the following questions: (1) How do major pension systems across the United States communicate financial, benefit and governance information to their members and other interested parties; and (2) Which retirement systems provide examples and lessons learned for how to effectively communicate relevant information?
- **Public Pensions Guide –** AARP, in collaboration with the Center for State and Local Government Excellence, has created a new public pension resource – Understanding Public Pensions – stressing the importance of elected officials understanding how public pension plans operate. The guide examines how state governments have pre-funded their pensions and reviews significant changes made to public pensions in recent years. It emphasizes the goals of all stakeholders: attracting and retaining employees; workforce management; retirement security; and keeping pension costs manageable. The guide examines the following: options for public pension plan design; the importance of adequate financing; how to develop a sound pension funding policy; important considerations when making changes to a pension plan; and the effects of various proposals on the workforce and employees and resulting financial effects.
- **Investment Returns of Public Pensions –** U.S. state and city pensions posted a median 4.1 percent return in the first quarter of 2017, marking the best performance since 2013. It was the sixth consecutive quarter of positive returns for public pensions. Improving economic conditions, stock market gains, and a weakening U.S. dollar helped bolster pension investments across the board. Larger pensions, which are typically more heavily invested in foreign stocks and bonds, performed better than the median fund. The gains will help ease the fiscal strain on state and local governments.

2. CalPERS Implications and Next Steps:

We will closely monitor and advocate against any pension related legislation that proposes PEPTA, the annuity accumulation plan, and/or could serve as a vehicle for similar anti-DB pension plan provisions.

3. CalPERS/Federal Representative Actions:

- The *ad hoc* public pension network, which is a group of stakeholders including NCPERS, NASRA, NCTR, NIRS, AARP and public employee labor unions, met on May 17. Your federal representative Tony Roda (Williams & Jensen) attended the meeting. Major highlights: (1) Congressional timetable is slipping for consideration of tax reform; (2) Enthusiasm in the House for a complete transition to mandatory Roth account contributions appears to be waning; instead, a proposal to allow pre-tax contribution up to 50 percent of an individual's annual contribution limit with the remainder as mandatory Roth contributions is under serious consideration; and (3) such an approach would not highlight the pick-up of state and local employee contributions as an anomaly.

- CalPERS' Assistant Division Chief for Federal Policy Gretchen Zeagler participated in three days of Congressional meetings (May 22-24) on CalPERS core legislative areas – retirement, health care and investments. Regarding retirement issues, Gretchen met with the staff of House Ways and Means Committee's Subcommittee on Social Security, and staff of Committee members Devin Nunes (R-CA), Mike Thompson (D-CA) and Judy Chu (D-CA) to discuss CalPERS priorities. Your Washington representatives Tony Roda (Williams & Jensen) and Tom Lussier (The Lussier Group) participated in the meetings. Of note, concern was expressed by Rep. Thompson's staff over the on-going possibility that a shift to mandatory Roth contributions could be included in the tax reform bill ultimately advanced by the Republicans. Such a shift is expected to include all defined contribution plans, including 401(k), 457(b) and 403(b) plans.

4. Recommendations for Next Steps:

CalPERS' retirement policy consultants, together with CalPERS staff, will be following-up on questions raised during Ms. Zeagler's visits and will be exploring opportunities for further engagement with the California Delegation and other key Congressional staff.

II. Developments in Advancing Retirement Savings and Retirement Security for All Employees

A. The Equal Treatment of Public Servants Act (H.R. 711 – 114th Congress) (Brady-Neal)

1. The Equal Treatment of Public Servants Act - would repeal the current Windfall Elimination Provision (WEP) of the Social Security Act and replace it with a new formula that will fairly account for covered and uncovered employment throughout an individual's career. The legislation will provide relief to current retirees whose Social Security benefits have been arbitrarily reduced by the existing WEP formula and, in general, will result in lower reductions for future retirees through the application of a new formula based on each worker's actual work history.

2. Specific changes/developments since last report:

   There have been no specific developments since the last report. *[NOTE – Based on conversations with staff for Mr. Brady and Mr. Neal, it's likely there won't be any developments on this legislation until later in 2017.]*

3. Implications for CalPERS:

   The passage of the Equal Treatment of Public Servants Act would offer relief to the thousands of CalPERS members who have been – or will be in the future – impacted by the WEP. Current retirees will see their WEP reduction reduced by approximately 15% for the first 10 years and up to 50% thereafter; on average, future retirees will see a reduction approximately 35% less than current law. These benefits have been updated based on a revised SSA actuarial analysis.

4. CalPERS/Federal Representative Actions:

   As noted above, CalPERS' Assistant Division Chief for Federal Policy Gretchen Zeagler met with staff of the House Ways and Means Committee's Subcommittee on Social Security to discuss CalPERS support for the Equal Treatment of Public Servants Act. In addition, she reinforced support for WEP reform in meetings with staff for Devin Nunes (R-CA), Mike Thompson (D-CA) and Judy Chu (D-CA).

5. Recommendations for Next Steps:

   CalPERS' retirement policy consultants will continue to communicate with staff for Chairman Kevin Brady (R-TX) and Ranking Member Richard Neal (D-MA) to coordinate activity in support for the Equal Treatment of Public Servants Act and will communicate with CalPERS staff to determine when additional engagement is appropriate.

B. Fiduciary Rule –

1. The Department of Labor (DOL) issued a rule that imposes a fiduciary standard on financial firms and advisers providing retirement advice. The rule will now become effective on June 9, 2017.

2. Specific changes/developments since last report:

   - Representative Phil Roe (R-TN) led a letter signed by 123 House Republicans urging DOL Secretary Alex Acosta to issue a further delay to the entire fiduciary regulation until the analysis required by the President's February 3, 2017 memo is completed.
   - On April 7, the DOL published an extension of the applicability date of the fiduciary rule and related exemptions to June 9, 2017.
   - In a surprising announcement, Department of Labor (DOL) Secretary Alexander Acosta said the agency could find no legal basis for further delaying the fiduciary rule and that the rule will take partial effect on June 9. Secretary Acosta emphasized that DOL has concluded that it is necessary to seek additional public input. DOL has issued a Field Assistance Bulletin and an FAQ Guidance for the transition period.

3. Implications for CalPERS:

   CalPERS has been supportive of the fiduciary rule. As a national and state leader in the retirement security arena, CalPERS has an interest in the implementation of the rule – especially as it might impact retirement security in California.

4. CalPERS/Federal Representative Actions:

   CalPERS retirement policy consultants will continue to monitor any activity regarding the rule and will communicate with CalPERS staff to determine whether additional engagement is appropriate.

5. Recommendations for Next Steps:

   There are no specific next steps at this point.

C. State-Based Retirement Programs –

1. The Department of Labor (DOL) finalized a rule to facilitate the creation of state and political subdivision-based retirement plans such as California's Secure Choice plan. The rule was intended to enable states to initiate innovative ideas that will boost overall retirement savings.

2. New Developments Since Last Report:

   - On May 3, the Senate passed H.J. Res 66, which disapproves the rule submitted by the Department of Labor (DOL) relating to savings arrangements established by states for non-governmental employees. The vote count was 51-48, with only two GOP Senators voting against the measure – Todd Young (IN) and Bob Corker (TN). The resolution would nullify the Department of Labor rule establishing safe-harbors from ERISA for state-run retirement programs for private sector workers.

President Trump has signed the resolution into law. *(Congress had previously passed and President Trump signed H.J. Res. 67, which nullified the DOL rule establishing safe harbors from ERISA for political subdivision-run retirement programs for private-sector workers.)*
- In the wake of the Senate vote to repeal the Department of Labor (DOL) regulation providing a safe harbor from ERISA for state-run retirement plans for private sector workers, Sen. Martin Heinrich (D-NM) introduced S. 1035, the Preserve Rights of States and Political Subdivisions to Encourage Retirement Savings Act (the PROSPERS Act). The new legislation would amend ERISA to specifically exclude from its scope certain IRA-based retirement plans run by state or political subdivisions for private sector workers. The bill has been referred to the Committee on Health, Education, Labor and Pensions for consideration.
- Despite the Senate action to repeal the DOL regulation, five states - California, Connecticut, Illinois, Maryland and Oregon - have indicated that they intend to move forward with their programs.

3. Implications for CalPERS:

   As a leader in the retirement security arena, CalPERS has an interest in efforts that will boost overall retirement savings, especially those that would impact retirement security in California. We will evaluate other opportunities for CalPERS to engage in this important national discussion.

4. CalPERS/Federal Representative Actions:

   CalPERS retirement policy consultants will monitor any activity regarding S. 1035, the PROSPERS Act, and will communicate with CalPERS staff to determine whether engagement is appropriate.

5. Recommendations for Next Steps:

   There are no specific next steps at this point.

D. Other Retirement-Related Legislation/Activity –

- **Pick Up Legislation Introduced –** On April 27, Rep. Diane Black (R- TN), who is the Chairman of the House Budget Committee and a member of the Ways and Means Committee, introduced H.R. 2187, which would permit the use of the pick-up in situations where existing plan participants are given an election between plans or plan tiers with different employee contribution rates. The bill would restore flexibility for plans that existed prior to the issuance of Revenue Ruling 2006-43. H.R. 2187 is identical to legislation that was introduced in the 113th and 112th Congresses by then-Rep. Loretta Sanchez (D-CA). Orange County had requested the legislation at that time.

- **Miners' Health Benefits –** Language in the omnibus spending bill extended retired miners' health benefits through September. Senate Majority Leader Mitch McConnell's (R-KY) office stated that Congress continues "to work on securing the permanent fix." Miners have been anticipating passage of legislation allowing transfers of unspent money from a fund for cleaning up abandoned mines to the United Mine Workers of America (UMWA) health benefit plan. Original proposals in this regard also included funding for shortfalls in the UMWA pension funds. We have been monitoring this legislation to determine whether pension-related measures will be contained in future legislation.

- **House Education and Workforce Hearing –** On May 18, the House Education and the Workforce Committee's Subcommittee on Health, Employment, Labor and Pensions held a hearing on Regulatory Barriers Facing Workers and Families Saving for Retirement. Topics discussed in the hearing included: (1) state-based retirement plans; (2) fiduciary duty rule; (3) open multiple employer plans; (4) retirement savings gap; (5) health care; (6) electronic delivery; and (7) annuities.

- **Pension Reform Legislation -** Senator Bernie Sanders (I-VT) and Rep. Marcy Kaptur (D-OH) introduced the Keep Our Pension Promises Act (KOPPA), S. 1076/H.R. 2412, which is designed to reverse provisions in the Multiemployer Pension Reform Act of 2014 that allow cuts to benefits promised to multiemployer pension fund participants. The bill also seeks to keep the Pension Benefit Guaranty Corporation's multiemployer pension program sustainable. Senator Sanders and nine other Democratic members of the Senate Health, Education, Labor and Pensions Committee sent a letter to Chairman Lamar Alexander (R-TN) asking for a hearing to discuss ideas for preventing the reduction of retirees' benefits and dealing with the multiemployer pension crisis.

III. Other Updates and Information

- **Puerto Rico –** After failing to reach a negotiated settlement with creditors, the federally-appointed financial oversight board filed in U.S. District Court in Puerto Rico to place the territory under protection from recent creditor lawsuits. The action is authorized by Title III of the Puerto Rico Oversight Management and Economic Stability Act (PROMESA). It provides a debt restructuring process similar to that available to certain municipalities under Chapter 9 of the Bankruptcy Code. The oversight board will now present a settlement plan to the court. A federal bankruptcy will be appointed to oversee the process. The current filing includes only the $18 billion in debt backed by the constitution of Puerto Rico. Additional debt is likely to be included in the restructuring process, including pension shortfalls.

  On May 17, a federal judge opened bankruptcy proceedings in Puerto Rico, which currently has almost $50 billion in unfunded pension liabilities and $74 billion in bondholder debt. Regarding pensioners, the federally-appointed oversight board's plan calls for a 10 percent cut in benefits, except for those below the poverty line. Also, new hires would be enrolled in defined contribution plans.

- **South Carolina Pension Bill –** South Carolina Governor Henry McMaster signed legislation aimed at shoring up the state's public pension plan while also calling for future revisions. Under the new law, public employee contributions will increase from 8.86 percent to nine percent in the fiscal year that begins July 1. Employer contributions will rise over six years from 11.56 percent to 18.56 percent. The Governor expressed disappointment that the law did not go so far as to implement a date certain transition from defined benefit pension plans to a defined contribution retirement plan for new state employees.

- **Houston Pension Petition –** A petition for a voter referendum has been submitted to the City of Houston calling for closure of its traditional defined benefit pension plan. Under the referendum, those hired on or after January 1, 2018 would be enrolled in a defined contribution plan. The petition comes while Houston Mayor Sylvester Turner is working to pass a pension reform bill in the state legislature.