THE LUSSIER GROUP, INC. WILLIAMS & JENSEN Est. 1970 | PLLC

Federal Retirement Policy Report for CalPERS Board
December 2016 - January 2017

I. Developments in Protecting Public Sector Defined Benefit Plans

Throughout the 114th Congress, CalPERS advocated against legislation that would advance the Public Employee Pension Transparency Act (PEPTA) and/or the so-called annuity accumulation plan. The final piece of legislation that was a threat to carry PEPTA and/or the annuity accumulation plan was funding relief for pension and health care benefits for retired coal miners.

1. New Developments Since Last Report:

- The coal miners relief legislation was narrowed in the final days of the 114th Congress to provide temporary funding relief only for the shortfall in the retiree health care trust fund – through April 28, 2017. Retirement issues were not addressed.
- Senate Majority Leader Mitch McConnell (R-KY) has introduced the Helping Ensure Long-term Protection for Coal Miner Health Act (S. 176) to provide permanent funding for retired coal miners' health benefits.
- The bill expands the eligible uses of interest transferable to the United Mine Workers health benefit plan from the Abandoned Mine Reclamation Fund. The Government Accountability Office would be required to audit the plan every three years.

2. CalPERS Implications and Next Steps:

As this new legislation moves through the 115th Congress, we will monitor it closely and advocate against the addition of any problematic provisions. Similarly, we will monitor any other 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 met on January 10 to discuss the upcoming Trump Administration and 115th Congress. Issues discussed included the need to work against the inclusion in tax reform legislation of PEPTA, the annuity accumulation plan and any other problematic proposals.
- Your federal representatives also continued an education and outreach effort to California Congressional Delegation offices. Meetings were held with staff of Reps. Devin Nunes and Mimi Walters.
- Your federal representatives also continued outreach and advocacy efforts in presentations to the National Conference on Public Employee Retirement Systems (NCPERS) (Tony Roda) and the Florida Public Pension Trustees Association (FPPTA) (Tom Lussier).
- Mary Anne Ashley, CalPERS Chief of Legislative Affairs, met with senior staff of the House Ways and Means Committee, Senate Finance Committee, and Rep. Mike Thompson's office during her participation in the NCPERS Legislative Conference.

4. Recommendations for Next Steps:

The CalPERS' retirement policy consultants will continue to monitor any legislation – such as the Helping Ensure Long-term Protection for Coal Miner Health Act – to prevent the inclusion of unrelated retirement provisions that would threaten the independence of state and local pension plans.

II. Developments in Advancing Retirement Savings and Retirement Security

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 provide a less significant reduction to future retirees.

2. Specific changes/developments since last report:

   - Although we expect the Equal Treatment of Public Servants Act to be reintroduced early in the 115th Congress, legislation has not yet been filed.
   - Rep. Kevin Brady (R-TX) will continue as Chairman of the Ways and Means Committee. Rep. Richard Neal (D-MA) has been elected to the ranking member's position on the Ways and Means Committee.
   - As a result of Xavier Becerra's departure from Congress, Rep. Mike Thompson – a co-sponsor of H.R. 711 in the last Congress – is now the most senior California Democrat on the Ways & Means Committee.

3. Implications for CalPERS:

   The passage of 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:

   CalPERS retirement policy consultants have continued to discuss WEP reform options with staff for Congressmen Brady and Neal; including the need for updated actuarial data to address specific questions raised by public employee and retiree organizations.

5. Recommendations for Next Steps:

   Discussions are underway to support the reintroduction of The Equal Treatment of Public Servants Act. We will continue to communicate with CalPERS staff as these efforts advance and will continue to include outreach to key members of the California Congressional Delegation as 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.

2. Specific changes/developments since last report

   - A federal judge in Kansas declined to issue an injunction that would block the Department of Labor's (DOL) fiduciary rule. Plaintiff, Market Synergy Group, alleged DOL violated the Administrative Procedure Act when midway through the rulemaking process DOL decided to regulate fixed-index annuities more aggressively than other annuities. The judge reasoned that Kansas-based insurance company was unlikely to prevail on its claim that the DOL used an improper process when designing the rule.

- There are currently six pending lawsuits challenging the rule. A federal judge in Washington, DC upheld the rule in a lawsuit brought by the National Association for Fixed Annuities. That decision is on appeal in the D.C. Circuit.
- On December 14, the ultra-conservative group of House Members, the Freedom Caucus, released a list of more than 200 rules and regulations for President-elect Trump to target in his first 100 days in office. Included in the list is the Department of Labor's fiduciary rule.
- Rep. Joe Wilson (R-SC) introduced the Protecting American Families' Retirement Advice Act (H.R. 355), which calls for a two-year delay of the implementation of the Department of Labor's fiduciary rule.
- The rule's future is unclear. In addition to the Wilson bill, Congress may use the Congressional Review Act to repeal the regulation. There is also discussion of using the regulatory process to authorize a two-year delay in the implementation of the rule.
- Sen. Elizabeth Warren (D-MA) wrote letters to the CEOs of 33 financial firms to ask whether they support delaying and rolling back the fiduciary rule.
- The rule is scheduled to take effect with partial compliance on April 10 and full compliance on January 1, 2018.

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) has finalized a rule to facilitate the creation of state-based retirement plans such as California's Secure Choice plan. The rule is intended to enable states to initiate innovative ideas that will boost overall retirement savings.

2. New Development Since Last Report:

   - On December 20, the Department of Labor published a final rule entitled Savings Arrangements Established by Qualified State Political Subdivisions for Non-Governmental Employees, thereby creating a safe harbor for certain large cities and other political subdivisions to create their own retirement plans. Cities and counties may only sponsor plans where there is no established statewide option and the population of the political subdivision must be larger than the population of the smallest state.
   - The New York City Comptroller established a retirement security study group to design a retirement program which was initially announced in October 2016.

3. Implications for CalPERS:

   As a leader in the retirement security arena, CalPERS has an interest in DOL rulemaking that will boost overall retirement savings; especially those that would impact retirement security in California. 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.

   In addition, given CalPERS believes that all employees should have effective means to pursue retirement security, we will evaluate other opportunities for CalPERS to engage in this important national discussion.

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.

III. OTHER UPDATES AND INFORMATION

1. Regulatory Freeze and Amendments to the Congressional Review Act

President Trump's Chief of Staff Reince Priebus released a memo on Inauguration Day to the heads of executive departments and agencies establishing a freeze in the issuance of any new federal regulations, except for those related to emergency or other urgent circumstances. The memo also directs that all regulations that have been sent for final review to the Office of Management and Budget but not yet published in the Federal Register be immediately withdrawn. For regulations that have been published in the Federal Register but are not yet effective, the memo requires that their effective dates be delayed for 60 days, with additional delays recommended in cases where there are substantial questions of law or policy.

Sen. Ron Johnson (R-WI) introduced a bill to amend the Congressional Review Act to allow the bundling of multiple regulations in one joint resolution of disapproval. Under current law, a resolution of disapproval can contain only one regulation and the resolution is subject to up to 10 hours of debate in the Senate. While the House has already passed the companion bill, called the Midnight Rules Relief Act (H.R. 21), it is unlikely the Senate will be able to secure the 60 votes needed for passage of the legislation.

2. CBO Report on Deficit Reduction Options

On December 8, the Congressional Budget Office released a report entitled, Options for Reducing the Deficit: 2017 to 2026. The report presents 115 options that would decrease federal spending or increase federal revenues over the next decade. The options are based on proposed legislation, budget proposals from various Administrations and private sector recommendations. The report includes options to further limit annual contributions to defined contribution retirement plans, including 457(b) plans (page 156) and expand Social Security coverage to include all newly-hired state and local government employees (page 169).

3. Implementation of MPRA

Pension plans looking to use the Multiemployer Pension Reform Act of 2014 (MPRA) to cut benefits and avoid insolvency should expect the Treasury Department and Pension Benefit Guaranty Corporation (PBGC) to test all actuarial assumptions used in developing proposals. The PBGC will also check every calculation made in the proposal to confirm it meets the technical requirements of the law. Iron Workers Local 17 Pension Fund was the first pension plan to have its MPRA application approved. While the Fund worked with Treasury and the PBGC to check all calculations and get clarification, it did not receive guidance from the agencies or suggestions on how the Fund could meet the requirements in MPRA.

4. **Public Pension Funding and Reforms**

In a January 4th article, *Institutional Investor* reported that some governmental pension systems are "clawing their way back to long-term solvency." The article explains how a growing number of plans have instituted reforms aimed at long-term survival, while others have gone even further, creating dedicated funding sources. The article states that one of the most successful reforms has been increased employee and employer contributions, which are often accompanied by the creation of dedicated funding sources. Kansas and Montana two such examples. Oklahoma and Louisiana have created so-called stabilization funds to bolster pension programs.

A brief published by the Center for State & Local Government Excellence found that, in the wake of the financial crisis, 74 percent of state plans and 57 percent of large local plans have cut benefits and/or raised employee contributions. Most reductions in core benefits affected only new employees. They included increases in age and tenure required to earn benefits and reductions in the benefit multiplier. Current employees commonly saw increased employee contributions and reductions to cost-of-living adjustments.

5. **Negative Report from ALEC**

The American Legislative Exchange Council (ALEC), a longtime and strident critic of public pension plans, released a new report examining the role of politics in pension reform. The report alleges that lawmakers and pension plan officials often prioritize their own agendas rather than doing what is best for workers. ALEC offers several recommendations for how to reduce these problems including model policies for prudent pension investment.

6. **Dallas Police and Fire Pension Fund**

Dallas' bond rating may be downgraded by S&P Global Ratings for the second time in as many years. The current AA credit rating was placed on CreditWatch, a step which indicates it may be reduced within the next three months. Dallas is facing a $7 billion shortfall in its police and firefighters retirement fund.
On December 5, Dallas Mayor Michael Rawlings sued the Dallas Police and Fire Pension System's trustees to prevent further distributions of funds from the Deferred Retirement Option Plan (DROP). The complaint alleges the trustees have violated their ministerial duties by "cannibalizing" the fund's assets instead of managing them according to sound actuarial principles. As of 2015, the overall fund had a funding ratio of 45 percent. According to the complaint, the over-withdrawal of DROP assets reduced the fund's life-expectancy by one-third.

On December 2, a Texas judge ruled against an injunction request against the Dallas Police and Fire Pension Board. Several employees were seeking an injunction to halt the board from enacting amendments to the pension fund. City and state officials have been urging the pension board to make immediate changes to the ailing fund, which is losing an estimated $3.3 million a month and has caused a downgrade in the city's credit rating. The plaintiffs argued the board illegally increased its membership from seven to 12 members and, therefore, should not be allowed to put forth a vote to stop withdrawals. For the plan amendments to be authorized, 65 percent of the beneficiaries must approve the changes.

7. Chicago Teachers Pension Bill

On December 1, Illinois Governor Bruce Rauner (R) vetoed legislation that would have earmarked $215 million from the state for the Chicago public school system. The Governor characterized the bill as a 'bailout' that would do nothing to address the wider structural problems in the pension system. Rauner said he would only support such a payment if Democrats in the state legislature negotiated on a bill to overhaul public sector pensions.

8. **Teacher Pension Benefits**

The Wisconsin Supreme Court declined to review a teachers' group's challenge to pension revisions imposed under a 2011 law removing public sector workers' collective bargaining rights. This affirms a Court of Appeals ruling from 2016 which upheld the authority of school districts and municipalities to unilaterally modify retirement benefits. In the lawsuit, the Neenah Education Association filed suit against the school board alleging the 2011 law does not allow the school board to unilaterally impose changes to previously bargained benefits. The teachers said the benefit adjustments would cause them to lose $68 million in retirement benefits.