February 26, 2018

Via email only

Re: State Pension Fund Recommendations

Dear Governor Hickenlooper, President Grantham, Speaker Duran and Honorable members of the Colorado State Assembly:

As an organization that represents over 3,000 employers and their 300,000 employees, the Denver Metro Chamber of Commerce is committed to growing retirement security for Coloradans. To that end, in May of 2017, we convened a diverse group of stakeholders with the goal of identifying strategies to improve the financial soundness of Colorado's defined benefit plan, the Public Employees Retirement Association (PERA). The purpose of this letter is to share with you what we learned during that process and provide recommendations for legislative action from the Denver Metro Chamber of Commerce and Metro Denver Economic Development Corporation, two of the organizations involved in the stakeholder meetings.

The group met regularly for nine months to discuss and understand the driving forces behind the $32 billion unfunded liability, identify solutions that could ensure the state fulfills its commitment to provide a pension while being fair to taxpayers, and propose changes to the governance structure that would help avoid the accrual of unfunded liabilities in the future.

The organizations that participated in our stakeholder group were: Bell Policy Center, Burgess Services LLC, Colorado Association of School Executives CASE, Colorado Education Association (CEA), Colorado Succeeds, Colorado WINS, D.A. Davidson, Denver Metro Chamber of Commerce, Denver Public Schools, Gary Community Investments, Grand Junction Area Chamber of Commerce, Metro Denver Economic Development Corporation, PERA Board members, PERA Retirees, Reason Foundation, Secure Futures, and Secure PERA. Additionally, the late Greg Smith participated as former executive director of PERA, to provide information about the PERA system. Also, Representative K.C. Becker and Senator Jack Tate attended the meetings of the group and provided guidance during the process.

Although participants in our group spent considerable time studying PERA and deliberated possible solutions, we did not reach consensus on recommendations. And, while the recommendations contained in this letter come solely from the Denver Metro Chamber of Commerce and the Metro Denver Economic Development Corporation, they were influenced from the time we spent with the participants in our process.

Below are the key long-term principles we believe should guide the legislature with regard to PERA:

LONG TERM GUIDING PRINCIPLES:

1. It is **critically important to make the necessary changes** that will improve the financial viability of PERA **this legislative session. Every year the legislature fails to act costs taxpayers more money.**

2. The State of Colorado **should maintain a defined benefit plan** as moving away from the current structure at this time would exacerbate the financial challenges. There is however, strong appetite for exploring benefit designs that would better meet today's workforce needs by providing a stronger blended pension model (defined benefit and defined contribution plans that add choices to both employers and employees and contribute to the unfunded liability).

3. PERA should aim to **achieve full funding by 2048 and maintain it into the future** (based on conservative return assumptions). We continue to be concerned that PERA's assumptions for its rate of return are too high and believe the plan should be fully funded in 30 years while constantly monitoring the actual returns and making adjustments to ensure it is fully funded by 2048. Fully funded plans are financially more efficient, less expensive for taxpayers and provide confidence to all stakeholders.

4. When considering benefit changes, it should be considered that PERA was established prior to Social Security and now serves as a **replacement for Social Security**. Members of PERA do not contribute to nor receive Social Security benefits for their years of service in PERA.

5. The **legislature should appropriate the actuarially required contribution each year** to avoid creating new liabilities in the future **or adjust the benefit levels down to support the appropriation it does make.**

6. In the future, corrective action must occur more quickly and efficiently to ensure the PERA fund doesn't fall so far behind. To avoid past pitfalls that got us to where we are today, we believe there should be even stronger **legislative oversight.** Such a structure would recognize the critical role of the legislature and its **fiduciary responsibility for PERA, while reducing the likelihood that funding is not sufficient to cover the benefits being offered and broadening the working knowledge legislators have of the PERA system.**

SPECIFIC RECOMMENDATIONS FOR 2018:

- The long-term goal for PERA must be **full funding as soon as possible but, given the financial situation**, we recommend that changes to the plan under the assumptions currently in place ensure **an amortization period of 30 years or less – *a closed amortization structure***.

- **Shared Responsibility Shared Sacrifice:** To solve the unfunded liability in PERA requires the **financial support of employers, current and future employees and retirees**.
    - With regard to employers, **changes to Section 125 must be counted** as part of an increase in the employer contribution to PERA. These changes require that the contribution rate is applied to the higher gross salary rather than the lower net salary.

- Employees **should not contribute** more than the normal costs, the cost of the benefits they will receive. Normal costs are currently 11 percent.
  - Further exploration should be given to reducing benefits for current employees recognizing that current employees are receiving much greater levels of benefits than either the employer or the employee have funded and the cost of that should be not solely borne by future hires.
  - There needs to be **more information and transparency around the employer and employee contributions separating those** that are going to cover normal costs from those contributions used to pay down the unfunded liability.

- **COLA Adjustment:** Current retirees must share in the responsibility and sacrifice necessary to fix the problem. Therefore, **a reduction in the Cost of Living Adjustment (COLA) is imperative**.

- **Retirement Age:** Because PERA is a replacement plan for Social Security, the **retirement age should align with the Social Security retirement plan**. It would be a reasonable adjustment to increase the **age of retirement** for all plan members and at a minimum raise the retirement age to 65.

- **Retirement benefits should be calculated based on more years of service** than the three years currently used. We believe all funds should move to a minimum of **five years** and believe that seven years is worth considering. The PERA board recognized the need to increase calculations for all divisions and recommended increasing to a five year calculation for all divisions currently at three years, and increasing to a three year calculation for the Judicial Division, which is currently at one-year.

- There must be **a structure and process in place at the legislature that is more responsive** when issues, particularly financial challenges, arise for PERA. The legislature is the only entity that can change benefits and funding for PERA, therefore we believe the legislature must improve its oversight and responsiveness when economic conditions require significant changes be made. We recommend the **legislature develop a committee devoted specifically to the oversight of PERA.** The "PERA legislative committee" would:
  a. Receive additional training and orientation regarding pension finance and PERA
  b. Review quarterly the soundness of PERA (both the levels of benefit and the funding)
  c. Share information disclosing the normal costs that will cover the benefits offered and the share of the contributions going to cover the unfunded liability
  d. If full funding will not be achieved by 2048, make additional recommendations to achieve full funding by 2048
  e. Thereafter, recommend changes to the plan to maintain full funding to the JBC and the General Assembly as part of each legislative session
  f. Ensure the PERA Board is administering PERA as mandated and make recommendations for the PERA Board structure as warranted. *(Note: we learned as part of our process that many stakeholders would also like to see changes in the PERA board itself. These stakeholders felt that the majority of the PERA board should NOT be made up of*

members who are vested in PERA and that they should have some expertise in financial matters and investing.)

As the largest unfunded liability in the state, we know that we must to make changes to PERA in order to secure a healthy financial future for participants in the program as well as our state budget. We believe the aforementioned recommendations provide a balanced approach to reducing the unfunded liability. We recognize that this will be an ongoing process that will require reevaluation and course correction when necessary and we urge the legislature to take on this challenge.

Thank you for your consideration and please feel free to reach out to us with any questions or concerns.

Sincerely,

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