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# *Committee Meeting*

of

## JOINT LEGISLATIVE COMMITTEE ON PUBLIC EMPLOYEE BENEFITS REFORM

*"The Committee will receive a presentation on legal issues  
related to changes to pension benefits by the Office of Legislative Services"*

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**LOCATION:** Committee Room 11  
State House Annex  
Trenton, New Jersey

**DATE:** August 23, 2006  
10:00 a.m.

### **MEMBERS OF JOINT COMMITTEE PRESENT:**

Senator Nicholas P. Scutari, Co-Chair  
Assemblywoman Nellie Pou, Co-Chair  
Senator Ronald L. Rice  
Senator William L. Gormley  
Assemblyman Thomas P. Giblin  
Assemblyman Kevin J. O'Toole



### **ALSO PRESENT:**

Aggie Szilagyi  
*Office of Legislative Services  
Committee Aide*

Christian Martin  
George LeBlanc  
*Senate Majority*  
Aaron Binder  
Karina Fuentes  
*Assembly Majority  
Committee Aides*

Laurine Purola  
Olga Betz  
*Senate Republican*  
Jerry Traino  
*Assembly Republican  
Committee Aides*

***Meeting Recorded and Transcribed by  
The Office of Legislative Services, Public Information Office,  
Hearing Unit, State House Annex, PO 068, Trenton, New Jersey***

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**ASSEMBLYWOMAN NELLIE POU (Co-Chair):** Good morning, everyone, and welcome to the second meeting of the Joint Committee on Public Employees Benefit Reform.

Our focus of today's hearing will center on the legal parameters of reforming our State's Pension system. We will be taking testimony shortly on a legal opinion the Office of Legislative Services has issued on the ability to make changes in the State's pension system.

On behalf of all of my Committee colleagues, I wish to thank our scheduled guests for preparing their presentation today.

I also want to make one thing abundantly clear at the outset of this hearing. This meeting is for fact-finding purposes. Now -- not three months from now -- is the time to establish the legal parameters that will determine the scope of reforms this Committee will be able to advance at upcoming hearings. It is this Committee's intention to be as thorough, comprehensive, and as ambitious as possible when that time comes.

The legal opinion that we're about to receive will help us in achieving the goals by better enabling us to separate the wheat from the chaff of potential reforms. No one said property tax reform was going to be easy to achieve, which is probably one reason why the previous Legislature found it preferable to ignore the issue entirely.

I think I speak for everyone on this panel when I say we are fully committed to doing the job we were chosen to do. Fact-finding is an important facet of that mission. It is my hope that today's testimony gives clarity to the parameters of this Committee, so that we do not waste precious time debating and discussing ideas that will not pass legal muster.

There may be some uncertainties about the specifics of the actual reforms this Committee will one day advance, and that is just the way it should be at this point. For all the members of this Committee, there should be only one certainty, and that is this: the status quo must give way to change if we are really about to achieve property tax reform. There's no escaping the fact that the financial distress of New Jersey's property tax system cannot be ignored any longer.

Ladies and gentlemen, thank you so very much for your attention.

At this time, I'd like to turn to my Co-Chairman, Senator Scutari, for any opening remarks.

**SENATOR NICHOLAS P. SCUTARI (Co-Chair):** Thank you very much, Chair.

If I could just remind everyone to please turn their cell phones to silent at this point in time, just so we don't have any interruption in the testimony when it goes forward.

First, I just want to thank the hundreds of members of the public that took the time to make thoughtful suggestions and submit them to the Web site for our review. This is, and will continue to be, a collaborative effort from all members of the Committee.

Over the next two days, we'll continue our education about this incredibly complex and very important topic. The Office of Legislative Services will walk through the statutory and constitutional issues that relate to the pension benefits that we must be aware of at the outset, so that we can continue to determine what alterations and changes this Committee is able to recommend. By establishing this legal framework, we will be better

able to focus the public's energies, and our energies, and these proceedings on pursuing practical remedies to our very real problems.

Tomorrow, the Director of the Division of Pensions and Benefits will discuss the current funding status of the pension systems. He will hopefully provide greater detail on the unfunded liability, on the major system changes enacted over the past 10 years that got us where we are today. Director Beaver will also respond to the Committee's request to review, prioritize, and make recommendations on the pension-related recommendations that were previously brought to our attention through the Murphy report.

Next week, we'll begin to discuss the differences between the defined benefit and defined contribution plans that we're considering. And in future meetings, we're going to open up the Committee to some public testimony and accept comments from members of the public wishing to testify. We will then move forward from pension reform to health and other benefits reform, with an eye on our mid-November deadline. It is crucial that this Committee receive an honest assessment of the current state of the pension systems, gather information from experts, and evaluate our options, and make suggestions that will ensure the viability of the public employee pension and benefits, going forward. And I think that's a very important thing that we have to discuss -- is continuing to have a viable system, going forward, in the future. And I think that's also a very real goal of this Committee. I believe that through this framework we'll be able to ensure that this Committee will produce some meaningful and lasting reform for New Jersey taxpayers.

Madam Chair, thank you very much.

ASSEMBLYWOMAN POU: Thank you, Senator. Thank you so very much.

As I pointed out, this meeting today is really on providing us the legal parameters. And while I may be focusing on the pension end of it, there is still going to be a lot of questions on the benefit side that -- clearly, we're going to want to get some further clarification and legal opinion on that as well.

At this time, I'd like to ask Mr. Peter Kelly, the special Principal Counsel to the Office of Legislative Services, if he would please come forward and provide his presentation to us. Is Mr. Kelly in the room? Oh, okay.

**P E T E R J. K E L L Y, E S Q .:** Good morning, Senator Scutari, Assemblywoman Pou, and members of the Committee. My name is Peter Kelly, and I am an attorney with the nonpartisan Office of Legislative Services. With me this morning is Pamela Espenshade, who is also an OLS attorney.

We are here today to discuss a legal opinion prepared by OLS for the Committee. We were asked to address the question whether the Legislature, by law, may reduce the retirement benefits that have been provided for public employees in the statutes, establishing that there is State-administered retirement systems.

For reasons which I will explain, it is our opinion that legislation that has the effect of detrimentally altering the retirement benefits of active members of State-administered retirement systems who have accrued at least five years of service, or of retired members, would be unconstitutional. And we believe this because it would be violative of the

Federal and State constitutional proscription against impairment of the obligation of contracts.

Our reasoning can be summarized briefly as follows: In 1997, the New Jersey Legislature enacted a statute that confers on a public employee a nonforfeitable right to pension benefits established by law after the employee has served for five years. In enacting that law, the Legislature intended to establish a contractual right. The Federal and State Constitutions prohibit the impairment of the contract, and therefore promised retirement benefits cannot be altered.

Before we discuss the statutory provisions in more detail, it may be helpful to view this issue in the context of New Jersey case law, and case law in other jurisdictions. The philosophy underlying public employee pensions has evolved. Older cases in New Jersey and elsewhere describe public pensions as a gratuity bestowed by a grateful sovereign upon a faithful servant for dedicated service. The more modern view is that a public pension is a form of deferred compensation to which an employee has a contractual right.

A majority of other states now take the view that public employees have certain contractual rights in a public pension where a pension is part of the terms of employment. The modern trend has been to protect pension rights on the theory that a state's promise of pension benefits represents an offer that can be excepted by the employees performance. In New Jersey, the courts have recognized that pensions for public employees serve a public purpose, in that a primary objective in establishing them is to attract and retain qualified employees. The New Jersey Supreme Court has acknowledged the evolution of the philosophy

underlying public employee pensions. But to date, the court has not found it necessary, in cases brought before it, which have primarily involved pension forfeiture for dishonorable service, to characterize the nature of a public pension as either a gratuity or a contractual right.

However, in 1997, the Legislature addressed this issue through the enactment of N.J.S.A.43:3C-9.5, which established for members of State-administered retirement systems a nonforfeitable right to receive benefits. The law provides that a member of a retirement system with five years of service on the Act's effective date, June 5, 1997, has a nonforfeitable right to receive benefits under the laws governing the retirement system on that date. A member accruing five years of service credit after the law's effective date has a nonforfeitable right to benefits based on the laws governing the retirement system on the date the member completes five years of service. In either case, the nonforfeitable right to receive benefits means that the benefits program for that member according from the statute cannot be reduced. The Act does not apply to post-retirement medical benefits or forfeitures for dishonorable service.

The enactment of that section of law also served to provide notice to persons beginning public employment after the law's effective date that their pension rights will not become unalterable until they accrue five years of service.

In general, a statute is itself treated as a contract when the language and the circumstances of it is a legislative intent to create private rights of a contractual nature, enforceable against the State. Both the United States Constitution and the New Jersey Constitution prohibit the enactment of laws that impair the obligation of contracts. These two

constitutional provisions provide parallel guarantees and are construed in the same way to provide the same protection.

When a state impairs a contract to which it is a party, the state's self-interest is at stake and the courts will more closely scrutinize the legislative assessment of reasonableness and necessity. In regard to the state's self-interest, the United States Supreme Court has noted that "a governmental entity can always find use for extra money, especially when taxes do not have to be raised. If a state could reduce its financial obligations whenever it wanted, to spend the money for what are regarded as an important public purpose, the contract clause would provide no protection at all."

The standard of review, that applies when the State passes a law that impairs a contract to which the State is a party, involves a two-step process: the first assessment is whether the State had the power to create irrevocable contract right in the first place, since the State cannot surrender an essential aspect of its sovereignty. The next step in the analysis is whether the impairment is reasonable and necessary to serve an important public purpose. Necessity is met if the objectives cannot have been achieved by a less drastic alternative. Reasonableness depends upon the extent of the impairment and upon whether the circumstances giving rise to the impairment were foreseeable when the contract was made.

When these standards are applied to legislation having the effect of reducing pension benefits to which, by law, nonforfeitable rights have attached, it is apparent that the State would be impermissibly impairing the obligation of a contract to which it is a party. There can be no doubt that the State has the authority to contractually obligate itself to

the payment of public employee pensions as a means of attracting and retaining well-qualified employees, and it has not thereby relinquished an essential aspect of its sovereignty.

In addition, public employees, who rely upon an offer of deferred benefits to their detriment and to the benefit of the employer who gains the employees service and loyalty, have expectations which are protected by the law of contract. Thus, any impairment of these rights would not be reasonable, given the expectations of the parties and the employee's detrimental reliance on the employer's representations. Nor would it appear that a reduction in benefits is necessary to prevent the financial collapse of the State, the only situation in which we believe the court may tolerate a detrimental alteration of contractual rights. A more modest means of savings or raising money are available to the State that do not affect contractual obligations. A reduction of promised benefits would effectuate an impairment to the State's responsibility under a unilateral contract that it created.

In addition, we believe that the circumstance could be raised that the need for proposed benefit reduction -- that the State, at a future time, may wish to reduce its financial obligations -- was foreseeable at the inception of the contractual relationship, and that the State nevertheless committed itself. There is a caveat to -- well, based on this, we have concluded that a law that has the effect of detrimentally altering the retirement benefit of an active member of a State-administered system who has accrued at least five years of service credit, or a retired member, would be unconstitutional, as I indicated at the beginning, because it would be

violative of the constitutional proscription against the impairment of contracts.

An important caveat to all this, which I wanted to mention, is that in many states that recognize contractual rights of a public employee -- in this state, a local pension system -- those rights are subject to reserved legislative power to make reasonable modifications to the plan or to modify benefits if there is a simultaneous, offsetting new benefit of greater or equal value. Thus, such a substitution of one benefit for another may be permissible without impairing the obligation of contract, as long as the change is reasonable and any disadvantage to the members is accompanied by offsetting and counterbalancing advantages. There is examples of that, which we can get into a little bit further, in other jurisdictions where, for instance, the retirement age was raised but the retirement benefit was simultaneously increased. And that was viewed by the courts as an appropriate counterbalancing.

Since we don't have a case on that point in New Jersey, we're not sure what the New Jersey courts would do, but it is an option that has been exercised elsewhere that New Jersey courts may recognize.

Some additional points: We believe that when a member has served and retired, all the conditions precedent to the receipt of a pension have been fulfilled and the member's benefits may not be changed to his or her detriment. So we're saying today -- is that the benefits, we believe, are protected for employees with five years or more of service, and also retired employees. We're also of the opinion that increases in benefits can become a contractual right. PL2001, Chapter 133: "Increased the retirement allowance of members of PERS and TPAF by changing the benefit formula.

Following the contract model, we believe that this increase represented a modification of the contract which, having been accepted by the members through their performance, also cannot be detrimentally altered.” And while it appears that the retirement benefits for members with fewer than five years of service could be detrimentally altered, implementation of any change may have to be limited to prospective application. That is because it would be inequitable, we believe, to rescind credit earned for the period prior to completing five years of service, and may affect property or implied contractual rights of the employees.

And let’s see -- one final point. We believe that Section 9.5, because it created contractual rights for the members to whom it applies -- that any subsequent amendment or repeal of that statute would not extinguish the rights conferred on those members.

So to summarize, it’s our opinion that the 1997 enactment confers on public employees a nonforfeitable right to pension benefits established by law, after the employee has served for five years. In enacting the law, the Legislature intended to establish a contractual right. The Federal and State Constitutions prohibit the impairment of a contract, and therefore promised retirements for those employees cannot be altered.

We will be happy to respond to any questions the Committee may have about the opinion.

ASSEMBLYWOMAN POU: Thank you, Mr. Kelly.

Let me just begin by asking: Is there an opinion, or do we know of any other state that has a similar law, in any other state that is similar to New Jersey, that has -- places a limit on the state’s ability to reform the pension system?

MR. KELLY: There are other states that have laws like that. I believe there are a half dozen that actually put such provisions in their state constitutions, including New York.

ASSEMBLYWOMAN POU: Do we know what they are -- what states they are?

MR. KELLY: No, but we can provide that.

ASSEMBLYWOMAN POU: Do we know if any of those states have taken any action towards attempting to change the laws?

**P A M E L A H. E S P E N S H A D E, ESQ.:** In some of the states that have laws or constitutional provisions that say that the benefits are frozen or contractual -- then make their changes prospectively. New York State, because it has a constitutional provision, when it changes any of its pension systems has provided basically a tier system, where you would draw a line. And prospectively everybody hired after a certain date would be-- Or some states that I think have changed some of their systems have made it voluntary to switch over to, say, a changed system when you're trying to offer a new value, and the person themselves could make the choice to change the contract that exists and move to a new system that might be offered to new people. And active employees might have the option of going over.

You have 50 states -- each state is a lot like New Jersey and has, perhaps, five or six pension systems. The city of New York alone has as many pension systems as we have, I think, and then the state of New York has a whole other set. So there's a lot of different specific things to look at if you were looking at all the states.

ASSEMBLYWOMAN POU: Thank you very much. Thank you.

Any members?

Assemblyman O'Toole?

ASSEMBLYMAN O'TOOLE: Thank you, Chair.

Thank you very much, and welcome Peter and Pamela. I've worked with Peter before, and sort of respect your opinion, both of your opinions, and have read through your opinion. But I have some, I guess, academic questions before we get into the meat of it. And let me just understand -- I assume this is through the Chair to Peter or Pamela: Your comment about extinguishing the 1997 law -- which you believe gave nonforfeitable rights, will not do anything to extinguish those nonforfeitable rights? Is that what you said?

MR. KELLY: For those employees to whom the right is attached by virtue of having five years of service.

ASSEMBLYMAN O'TOOLE: Prior to the 1997 law, did these nonforfeitable rights exist, implied or otherwise?

MR. KELLY: We don't have a court decision on that point in New Jersey, the reason being that I don't believe the benefits have ever been reduced before. Therefore there has been no lawsuit on that point and, consequently, no court decisions. The expectation is, perhaps, that if the New Jersey courts had to confront this issue in the absence of the statute, that they would follow the majority rule, we think, in other jurisdictions, which establishes a common law right, in a contract, to a pension.

ASSEMBLYMAN O'TOOLE: While there's a series of Appellate decisions, the New Jersey Supreme Court does not answer, on point, this nonforfeitable right issue, correct?

MR. KELLY: Correct.

ASSEMBLYMAN O'TOOLE: Okay. So we really don't know. We believe, given what other jurisdictions have done -- we have a feeling, one way or another, as to how this Supreme Court would react.

But just from an academic standpoint, Peter, I'm trying to understand that if this right was given through a 1997 statute, passed by the Legislature and signed by the governor, how does that morph into a constitutional protection that cannot be erased by a retraction of that 1997 statute?

MR. KELLY: Because the statute itself, depending upon the circumstances under which the Legislature enacts it, if the Legislature -- if it's an intent to bestow a contractual right, the statute itself can become contractual.

ASSEMBLYMAN O'TOOLE: At that time?

MR. KELLY: Yes.

ASSEMBLYMAN O'TOOLE: But not--

MR. KELLY: But once a statute is-- If you give a statute bestowing a contractual right, then the State cannot impair that right.

ASSEMBLYMAN O'TOOLE: Okay. Subsection E of the statute that was passed -- N.J.S.A.43:3C-9.5 says, and let me just quote: "Accept as expressly provided herein, and only to the extent so expressly provided, nothing in this act shall be deemed to, one, limit the right of the

State to alter, modify, or amend such retirement systems and funds.” What does that mean?

MR. KELLY: I believe that that would make no sense -- if they were to bestow a benefit in the first two paragraphs and then take it away in the last paragraph; that I think that that language would have to be read as meaning that you can make alterations to the system or the fund itself. For instance, you could change how your investments are invested -- or how your assets are invested, the presumed rate of return -- things of that nature -- the structure of the system, as long as you're not affecting benefits.

ASSEMBLYMAN O'TOOLE: Do we have the legislative history-- It seems to me, it seems as we read that statute, there seems to be some clauses in conflict, or seemingly in conflict.

MR. KELLY: There is, unfortunately, no legislative history that sheds any light on the statute. This particular section was added by a committee amendment to a bill which was to conform certain aspects of our pension systems with requirements of Federal law. And there is nothing in the formal legislative history that explains why this provision was added.

ASSEMBLYMAN O'TOOLE: The next question is the analysis that needs to be done -- looking through the lens of the standard of review -- as to whether impairments brought about by State action are, in fact, reasonable. Could someone make the argument or-- For public purpose, could someone make the argument that solvency of the State of New Jersey is an important public purpose?

MR. KELLY: I believe only if we're on the verge of complete bankruptcy of the State. There's case law in other jurisdictions. In New York, the state tried to -- the state acted contrary to a negotiated collective

bargaining agreement by reducing the pay of the employees by 10 percent, with the promise that they would be paid that amount upon retirement. And the court said that the state of New York was not on the verge of becoming a failed state and therefore it could not abrogate its contractual responsibility.

ASSEMBLYMAN O'TOOLE: The question-- And this is the core of the question that I have, and I don't think we really have the answer. But when we talk about nonforfeitable right, is the nonforfeitable right the right to receive a pension?

MR. KELLY: No. The statute, I think, makes it clear in Subsection B that what you're entitled to is what has been promised in statute, either on June 5, 1997 -- the Act's effective date -- if you had more than five years of service, or on the date that you accrue five years of service. So whatever is provided by law at that point is what you are guaranteed.

ASSEMBLYMAN O'TOOLE: All right. Let's go to that question. The tacking/stacking issue, which we've read so much about, which to me is symbolic of some of the problems -- hard-working folks who have worked 18, 25 -- \$30,000 a year -- and have a expectation. I understand what that expectation -- I understand the contractual nature of the expectation, and what they should be receiving. What I don't understand: In 1997, was there an expectation or an understanding about -- say an individual worked for five different municipalities, making \$50,000 a year, and he or she is accruing 250,000. If that individual is in our system today, and we pass a bill tomorrow and sign into law next week, that individual can pull from just one town or is prohibited from having those

type of arrangements to count towards his pension -- are you saying we are precluded from stopping those type of abuses for an individual who has more than five years?

MR. KELLY: What you're trying to describe is multiple pension memberships.

ASSEMBLYMAN O'TOOLE: Sure. Or multiple -- no -- multiple jobs for one pension.

MR. KELLY: Well, when you hold multiple public jobs, you're enrolled in -- you have multiple enrollments in PERS and-- The point that I think would have to be made there, or that applies in general here, is that you can make changes that are prospective in application, you reduce the risk of litigation -- the potential litigation risk there, if you were to tell somebody who has three enrollments in PERS that they have to pick one of those three.

ASSEMBLYMAN O'TOOLE: And someone with more than five years, is that -- even when we say, going forwards. Day one, tomorrow starts, you can no longer draw from two different salaries. Someone who has, say, 10 years in the system, is that constitutionally protected, that we can make those reforms?

MR. KELLY: Well, I guess the test is whether or not you're detrimentally altering benefits. And if you're telling somebody who is holding, let's say, two public jobs, for simplicity sake--

ASSEMBLYMAN O'TOOLE: Right.

MR. KELLY: --that they have to choose one of those for their PERS membership--

ASSEMBLYMAN O'TOOLE: Right.

MR. KELLY: Then you're having an impact on the benefits that they'll be entitled to down the road. I mean, that may not be as clear an example as would be an across-the-board, 10-percent cut in the retirement benefit available to all PERS members. It may be a more gray area. I guess what I was suggesting was that the best approach to that would be prospective application, so that you would say, essentially, that if you have more than one PERS enrollment, you can keep that. When one of those jobs ends, and you only have one PERS enrollment, you are prohibited from thereafter picking up an additional PERS enrollment through additional public employment.

ASSEMBLYMAN O'TOOLE: Okay. I just think this is -- the pension has gone wild, but I'm trying to understand. This is an amorphous, moving, untested, judicially challenged concept. So we're really in unchartered water.

MR. KELLY: I share your feelings.

ASSEMBLYMAN O'TOOLE: Okay.

The last question, Chair -- I appreciate the latitude.

In your conclusion, Peter, you say -- and let me just quote the first line: "In conclusion, it is our opinion that a law that has the effect of detrimentally altering the retirement benefit of an active member of a State-administered retirement system who has accrued at least five years, or a retired member, would be unconstitutional as violative of the Federal and State constitutional proscription." My question is: In a larger sense, if by altering the pension for current employees we are saving the pension system and making it financially viable, could one argue in court that that would not be detrimentally impairing, but rather shoring up their pension system?

MR. KELLY: No, I don't think that argument would be successful. I think the State has the responsibility, under this contractual right, that it conferred to pay the pension. And whether that would have to be done with general revenues in the most dire circumstances, that's still the State's responsibility under the contract. The only case, we believe, in which the court would permit a modification to contract on those grounds would be if the State was on the verge of financial destruction. And I think that similarly would apply to the pension fund. The pension -- you know it's-- Depending upon how you assess the pension funds or look at them, they're either in good shape or not so good shape. I don't think we're at the point now where a court would find them in sufficiently bad shape that it would justify impairing the contract.

ASSEMBLYMAN O'TOOLE: Okay.

Thank you very much.

Thank you, Chair.

ASSEMBLYWOMAN POU: Senator Gormley.

SENATOR GORMLEY: First of all, to deal with the issue of prospective again, to follow up on Assemblyman O'Toole's point. Let's say someone's got multiple jobs. Going forward, you're saying even though I don't affect the accrued pension benefit of someone -- I'm not going retroactive -- there is still a question as to whether we can limit, prospectively, the tacking of these pensions together. Is that a fair characterization?

MR. KELLY: Yes. I think that question is there.

SENATOR GORMLEY: I guess the important part about the legislative history is, as the Assemblyman pointed out, it would not appear

that this was one of the reasons why this safeguard was given in 1997. And consequently, if you could refine this point even more, because we're not-- We're talking a circumstance that I don't think was envisioned by -- for whatever reason that passed in '97.

In terms of your opinion, I want to be very-- It's a statement of what I think is obvious, but let's go through it. When you are talking benefits in this opinion, you are only talking pension benefits. Is that correct?

MR. KELLY: That's correct, Senator.

SENATOR GORMLEY: Consequently, the safeguards that you are talking about from 1997, and whatever, do not affect health benefits. Is that correct?

MR. KELLY: Those safeguards apply to pensions.

SENATOR GORMLEY: Okay.

MR. KELLY: We're not--

SENATOR GORMLEY: Okay.

MR. KELLY: --prepared to speak to the issue of health benefits today, which is a separate and different issue.

SENATOR GORMLEY: Okay. Well-- But, therefore, it only applies to pensions -- the safeguards that you've mentioned.

MR. KELLY: We've only researched the pension issue.

MS. ESPENSHADE: Since you mentioned the date 1997, if you are referring to the statute, the statute specifically says it doesn't apply to health benefits.

SENATOR GORMLEY: Okay.

In terms of the “n/55,” the 2001 bill, if we were to change it back to “n/60” prospectively, what you’re saying is, even though we wouldn’t affect accrued benefits, we could not change that, moving forward, in terms of what would accrue. Is that a fair comment? Suppose we bifurcated it? We said we acknowledge that it existed for five or six years, or for those years that it had accrued up to that time. But prospectively, afterwards, the years afterward would be “n/60.” Could we do that?

MR. KELLY: You could not change it back to “n/60” for employees who have accrued five years of service.

SENATOR GORMLEY: What I’m saying is, if you included that five years or all the years of service to that point, could you, for the years after the date of the passage-- I’m not talking retroactivity; I’m talking prospective, from the date of passage -- could you have it bifurcated?

MR. KELLY: So what you’re saying is, if an employee has 10 years, then those 10 years would be calculated--

SENATOR GORMLEY: Absolutely. Absolutely.

MR. KELLY: --“n/55” or-- Right.

SENATOR GORMLEY: But going forward, I’m talking-- You see, I think we acknowledge your opinion. What we’re talking is, what does *prospective* mean now?

MR. KELLY: Okay. I don’t believe that you could change -- for employees for whom the nonforfeitable right has attached, I don’t believe you could change the formula for a time forward -- moving forward from this point. That for them, the formula would have to stay at “n/55.”

SENATOR GORMLEY: Okay. Have you been-- Are you working on an opinion related to health benefits?

MR. KELLY: Well, I wouldn't be at liberty to say if I was, because requests for opinions are confidential. If we are asked, then we will certainly work on such an opinion.

SENATOR GORMLEY: Thank you.

ASSEMBLYWOMAN POU: Senator Scutari.

SENATOR SCUTARI: Thank you.

I just want to get back to the point, for one moment, that Assemblyman O'Toole brought up -- this inconsistency with the statute that we've been talking about, the 1997 law; which is, specifically, Paragraph E. And it basically says fairly clearly that "nothing in the Act shall be deemed to limit the right of the State to alter, modify, or amend such retirement systems and funds." What you're saying is, that portion of the statute is not an arguable position that the State could take in amending anything?

MR. KELLY: I think you have to read the entire section of law. And in Paragraph A, it defines a nonforfeitable right as meaning that for any employee for whom the right has attached, benefits cannot be reduced. So I think that they're conferring that right in the beginning of this section. And at the end, it's not taking away that right, because that wouldn't make any sense. That would be an absurd result in interpreting the statute. I think at the end it is simply intended to make it clear that the State has latitude to rearrange the administration of the pension systems, but not the benefits.

SENATOR SCUTARI: It does seem clear, though, that although the statute does exactly what you say it does and gives a nonforfeitable right to these certain employees, doesn't at the end of the

statute it say, exactly, that although we're conferring that nonforfeitable right, they reserve the right to change that in the future?

MR. KELLY: I don't believe that that's what that section was trying to say there. I think it was trying to confer the right or reserve the right to the State to change things with respect to pension systems other than benefits.

SENATOR SCUTARI: Would you believe that there is an articulable argument that could be made based upon Section E, or do you not even believe that that's an argument that would even stand any chance of scrutiny?

MR. KELLY: No.

SENATOR SCUTARI: Okay. I guess that's pretty clear.

And just to follow up on Senator Gormley's remarks. It's in your estimation that a change with the "n/55" to "n/60" could not be changed for people already in the system with over five years -- even if, what the Senator suggested, we would use the 55 over number for the years that they were in the system, and then change it to 60 for other years that they're in? You don't believe that that can be done?

MR. KELLY: Right.

SENATOR SCUTARI: But it would only be able to be changed for people with less than five years in the system or people that are not yet working?

MR. KELLY: Yes. New hires and people with less than five years of accrued credit in the system.

SENATOR SCUTARI: But you would suggest that the Legislature has wide latitude to change benefits for people with less than five years, or people who are not yet in the system who aren't working yet?

MR. KELLY: Yes. We think prospectively there may be some concern. For instance, that someone who has three years to date, that there may have to be some recognition of that credit in whatever change you make. And the example we give in the opinion is, if you were to change for those employees the formula for calculating benefit from "n/55" to "n/60," what you may want to do is, when they retire, let's say 30 years from now, their benefits will be calculated with using three years over 55 and then 30 years over 60.

SENATOR SCUTARI: Isn't that exactly the suggestion that Senator Gormley made to--

MR. KELLY: No. I didn't think so.

SENATOR GORMLEY: Well, if the answer is "yes," it's the one I suggested.

MR. KELLY: I'm sorry if I misunderstood you, Senator.  
(laughter)

SENATOR GORMLEY: If it's a yes answer, it's the one I suggested. (laughter)

MR. KELLY: Yes. We're only talking about people with less than five years. That they may just want there to be some recognition of-- And once again, to avoid litigation, some recognition of what they've accrued thus far in whatever new system you were to devise for them, going forward.

SENATOR SCUTARI: Since we're on that initiative, one or two more follow-ups. What does the '97 law provide that isn't already in place for employees with less than five years of service? Does it provide anything?

MR. KELLY: No. It confers the benefit on people with five years on the Act's effective date, or people who accrued five years thereafter.

SENATOR SCUTARI: So then the opinion that you're giving, with respect to someone who has a three-year service -- that we were just talking about -- that would not be based on anything in the '97--

MR. KELLY: That's not based upon the statute. That's just based upon general notions of equity fairness.

SENATOR SCUTARI: Understood.

MS. ESPENSHADE: And also to recall that, if absent the 1997 statute, you still have all the underlying case law that is relied upon if a court was looking at these different situations-- We pointed out that before the statute there's the case law in different states, and other courts that have used this, that there is an expectation a property right develops. That does not disappear with the passage of the '97 law. The '97 law is sort of an articulation of that right. But for those first five years, that would still be part of the whole, more broad concept that once you start employment, you're developing an expectation, or a property right.

SENATOR SCUTARI: These constitutional arguments that are made prior to that 1997 enactment, and obviously supplemented by it, are not akin to private sector plans, are they? Would those same protections be

given to private sector plans? I mean, specifically the 1997 law targets public employment, does it not?

MR. KELLY: Yes, of course.

SENATOR SCUTARI: And it's not necessarily -- it couldn't be utilized by a private-sector type of benefit. There are pensions in other private sector -- large corporations provide a pension.

MR. KELLY: The State does not regulate those.

SENATOR SCUTARI: And so your suggestion is, obviously-- I mean, it's fairly obvious to me. But I just want to make it clear that these things that we're talking about are narrowly defined with respect to public employment and not private employment. Because there's been litigation that's gone on nationally, with respect to pensions.

MR. KELLY: They apply to public employee retirement systems.

SENATOR SCUTARI: Thank you.

ASSEMBLYWOMAN POU: Senator Rice.

SENATOR RICE: Yes, how are you doing?

MR. KELLY: Good morning, Senator.

SENATOR RICE: Could you kind of elaborate a little bit more on this area of substituting these benefits? If I'm reading and hearing you correctly, read the document, the courts are treating these pension obligations as legally binding contracts. Is that correct?

MR. KELLY: I'm sorry, the legislation is legally binding?

SENATOR RICE: The courts are treating pensions as legally binding contracts, if all the elements of a contract -- the quid pro quos, and things of that nature. Is that right?

MR. KELLY: Yes, that is true. The majority--

SENATOR RICE: I do something for you, you do something for me -- expectations, etc. Right?

MR. KELLY: Correct. That's true in the majority of states.

SENATOR RICE: And are we not saying -- and courts aren't saying-- Are not the courts saying that if, in fact, we intended to change some of these things as a government, we should have reserved those rights? In other words, anything that's foreseeable, we should address it from that perspective?

MR. KELLY: I guess what you're getting at, Senator, is the simultaneous offsetting of reduction of one benefit by an increase in another. We're not sure how that will be viewed by the New Jersey courts, just that that has been done and approved by the courts in some of the states that recognize a contractual right of employees to a public pension.

SENATOR RICE: And is there is a difference in definition of *modification* versus *change* in general, as it relates -- from a legal perspective?

MR. KELLY: A subsequent modification of the contract by the employer or--

SENATOR RICE: Yes.

MR. KELLY: We think, based on what we said with respect to the formula change, that changes that do not detrimentally alter the benefit for an employee -- in fact, increase the benefit -- can become part of a contractual right.

SENATOR RICE: Okay. Then if, in fact, I receive a pension presently, is that saying that whatever those benefits are-- If, in fact, I

change the system to something else, the benefits have to be equitable or greater?

MS. ESPENSHADE: Well, the -- I think the opinion says that the-- Again, because we don't have any case law in New Jersey, per se -- but the other states that have looked at this issue have said you examine whether somebody is adversely affected. And so it would be what you said. If you want to change something, or modify something, then you look at that modification or that change. And presumably a court -- which has happened in some specific instances that we've seen cases of-- They would look to see if they think that there is a counterbalance. You have two changes. One might be viewed as adverse, another one might be viewed as advantageous. So, in that sense, you would have a modification, but you'd have a balancing. But, again, this is only what is the basis of what we can base our opinion on, which is cases that have been in other jurisdictions.

SENATOR RICE: Well, if we're going to the theory that there is no net loss, then that sounds like an equity issue to me. If that's the case, how do we really save by changing the systems? In other words, if I'm due \$50, you're going to change the system -- I'm due \$50 or more. I mean, I'm trying to figure out, when we talk about other systems, whether they're 401s or something else, what are we really talking about, in terms of making sure there is no net loss, no substantial impairments; we are holding true to all the various elements that you pick up in law school, in contracts, in the first year, including reliance and expectations. How do we get around that, from your perspective?

MS. ESPENSHADE: An example we noticed recently -- I think it's-- Pennsylvania has made a change. And they did something like, they

increased the percentage that the employees contribute in one of their systems, but countered with increasing the benefit by a certain amount.

MR. KELLY: That was also voluntary.

MS. ESPENSHADE: And they did this prospectively, for new hires. And they also gave current hires the opportunity to move over to that new system. You have, again, this line between people who are in the contractual relationship, who already are active employees and have these expectations, and you have people who haven't entered into that relationship. And they don't have any expectations until they actually become employed.

The state of Michigan created a defined contribution system. And what they did was, they created a defined contribution system and had a defined benefit system. The people -- on the day that happened in 1997-- It wasn't just the day, they were given a period of time. Those people who had been functioning in their defined benefits system had the choice of staying in that -- and they are still in that if they so chose -- or they could join the new defined contribution system. And all the new employees hired after a certain date in 1997 are in that defined contribution system. And the choice to move over was irrevocable. So the people who had that choice would have been making the kind of equity and balance thing, looking at the advantages of the two systems and -- because the benefits aren't easily lined up.

And so when you have changes, you almost have to-- They don't necessarily line up dollar for dollar when they've had voluntary move-overs. It may depend on how long someone is going to work, what they visualize their career being. And so these modifications or counterbalancing

things wouldn't necessarily be, obviously, matched up. But in examining the adverse and the element of detriment, you would say that there seems to be a balance, and it's okay.

SENATOR RICE: Through the Chair, that system would have to be -- cannot be a mandate? It's voluntary -- own volition. Is that correct? The system you just described--

MS. ESPENSHADE: Well, because what we've said is that the relationship -- the contractual relationship -- the expectation has been set for the active employees. That's what the opinion says. So if you do create a new system for new people, you don't have to, but you may choose-- I believe the Department of Transportation -- not Department -- New Jersey Transit, in New Jersey, has a situation where they are trying to encourage some of their employees to go to a defined contribution system. And it's on-- New employees come in and join one system. And that system is available for people to move over to.

SENATOR RICE: And if they don't, there may not be any substantial changes. We're right back where we started with a fund that's now depleted.

Is there a difference, through the Chair, of-- Let's put it this way. The opinion draws -- seems to draw a distinction between an active employee and a retiree. Can you kind of go through that a little bit -- with less than five years? It seems that we need to know some of the rationale for that distinction and get some clarity on it.

MR. KELLY: I think the answer, with respect to retired employees -- and you'll find this pretty much universally in court decisions from other jurisdictions -- that when a member has served and retired, all

the conditions present at the receipt of the pension -- the contracts have conditions. All the conditions have been fulfilled, and the members benefits cannot be changed.

So I think that-- I don't think anybody has tried to change benefits for people who are already -- from public-administered systems -- who are already retired, because it's probably the clearest case in which the contract has come to fruition and been fulfilled.

And with respect to the employees with -- active employees with more than five years experience-- We're relying on the '97 statute as providing this nonforfeitable right. There are a number of states that don't have a statute like that where the courts have, nevertheless, recognized a contractual right. It's an implied, in fact, unilateral contract. When the public employer offers public employment, one of the conditions of which is, "You work here for 30 years, and you're age 60, you will receive a pension." The employee accepts the offer, through their acceptance of the employment and performance of the job. So even without a statute, you have, in some jurisdictions, a situation where the courts have determined a contractual right.

What they vary upon is the point at which that right attaches. Some view the employee as having a contractual right on the first day of employment. There are some others, which are probably extreme cases, where the contractual right isn't viewed as becoming guaranteed until you reach retirement age.

In New Jersey, we have the statute that pegs it at five years. If we didn't have that statute, our courts may still recognize a contractual right. And where they peg the point to which that right attaches, we can't

speculate on. It could be the first day of employment, it could be the point of vesting at 10 years, or something else. So there could be rights, under common law, outside of what's provided by the statute. So I think retirees are a pretty clear case. Active employees -- the five-year thing is specific to New Jersey because of the 1997 enactment.

Does that answer your question?

SENATOR RICE: Pretty much so. It gave me more clarity.

That's is for now, Madam Chair.

ASSEMBLYWOMAN POU: Thank you, Senator Rice.

I just want to make mention of something that Senator Rice was just talking about and, Mr. Kelly, what you had just responded to -- your last statement.

On Page 4 of your opinion, you make reference -- on the first paragraph, it reads as follows -- which probably talks about what you're now referring to. It says, "Although it appears that the retirement benefits for members with fewer than five years of service could be detrimentally altered, implementation of any change may be limited to prospective applications, the rescission of any credit earned for the period prior to completing the five years of service being problematic." And I presume that's the area that you were just talking about then. Is that correct?

MR. KELLY: Well, that obviously is applying to employees with less than five years of service.

ASSEMBLYWOMAN POU: Well, that's exactly what I'm referring to.

MR. KELLY: But the courts may recognize that what they have accrued so far -- at the point that you change the law -- can't be just wiped away, that there has to be some sort of recognition according to that.

ASSEMBLYWOMAN POU: All right. I just wanted to reference the section in your legal opinion -- that you're making reference to -- that speaks about, Senator, what you were just referring to.

Thank you, Mr. Kelly.

Assemblyman Giblin.

ASSEMBLYMAN GIBLIN: Mr. Kelly, I asked for a copy of this legislation going back to '97. And just for the benefit of the audience, this legislation was introduced by Senator Inverso and, on June 5, 1997, signed by then-Governor Christine Todd Whitman. Both Houses approved the measure by substantial margins. There was only a few dissenters.

But looking at the synopsis of the bill -- what the intent was -- it says, "conforms administration of certain State-administered retirement systems and pension plans to Internal Revenue code requirements." In your opinion, I noticed that you leave out a section about the contribution requirements on the part of the State. And I will just read it to you. "The State shall make an annual, normal contribution and an annual, unfunded accrued liability contribution to each system or fund, pursuant to standard actuarial practices authorized by law, unless both the following conditions are met: One, there is no existing unfunded, accrued liability contributions due to the system or fund at the close of the evaluation period, applicable to the upcoming fiscal year. And, two, there are excess evaluation assets in excess of the actuarial accrued liability of the system or fund at the close of the evaluation period, applicable to the upcoming fiscal year."

This issue about trying to conform to IRS requirements-- I know this is maybe something you're not prepared to answer today. But, going forward, the number we've heard at previous sessions has been an 83 percent funding, as far as the plans are concerned. I'm looking at this legislation. I know it's geared towards private sector pension plans. But one of the requirements with this new legislation is that plans in the private sector will have to meet full funding over a period of seven years. So if the intent here was to adhere to IRS requirements, I think the State has to look at this issue about how they're going to deal with this unfunded liability.

But another issue I'd like you to look at, too, is: Who, in fact, had the responsibility to make sure those contributions were made? Was it the trustees of the pension plan, was it the director of pensions, was it the State Treasurer? I mean, it seems to me-- I go back to this issue of fiduciary responsibility. If I'm a trustee of a plan and I know I have legislation on the books, and I'm not collecting the money, I'm liable.

MR. KELLY: A couple points, Assemblyman: First of all, the legislation, as introduced, said that it was for the purpose of complying with certain Federal requirements. The section, that became Section 9.5, was not part of the bill as introduced. It was added subsequently by a committee amendment. And it's not clear to us. We don't believe that that section was necessary to comply with any Federal requirement. It was simply an amendment to the bill so that, initially, the bill going in looks like it complies with Federal law. It's amended in this way, thereafter, and perhaps not necessarily because there was any Federal mandate -- that we amended in that regard.

With respect to the funding -- the appropriation of money -- we omitted that in the opinion for brevity sake, with an ellipsis. But I think that the answer to that is, there's any number of statutes that require the Legislature to appropriate money. And all those -- a lot of those, rather, are overridden, annually, by the annual Appropriations Act, which overrides any existing law. So if the Legislature, in enacting the annual Appropriations Act, chose not to provide for an employer contribution to the pension system, that would be what's controlling, no matter what the permanent law says.

ASSEMBLYMAN GIBLIN: In other words, we have the flexibility to interpret the laws to our convenience?

MR. KELLY: The Legislature has a lot of latitude with the annual Appropriations Act. It's a matter of not being able to tie the hands of future Legislatures with regard to the appropriation of money.

ASSEMBLYMAN GIBLIN: So, going forward-- I mean, the Governor and the Legislature appropriated -- what was it -- \$1.3 billion this year. We're under no obligation next year to do funding?

MR. KELLY: Well, you probably -- you may have a contractual obligation. That's debatable and perhaps the subject of litigation, as to whether or not the State has a contractual obligation to appropriately fund the pension systems. But there were, I believe, nine years where the employer contribution to the pension systems was not made, notwithstanding whatever the existing law -- the permanent law provided.

ASSEMBLYMAN GIBLIN: Well, it said each year that -- based on an actuarial study. And that's one paragraph here. At the close of

the evaluation period, you're supposed to have an actuarial study. Do we have actuarial studies every year? I know that's not your domain, but--

MR. KELLY: I think Pamela has that.

MS. ESPENSHADE: The pension statutes for each of the systems has that language. That language is referring, basically, to the statutory language that already exists, that at the end of each year the employer obligations are calculated. And those are numbers similar to the one that Chairwoman Pou asked for, when she was referring to the local obligations for one of the pension systems -- what was 40 percent, or 20 percent, or 100 percent.

So the calculations are made by the actuary in each of the pension systems as to how much is due. Defined benefits systems are based on taking in a set amount from the employees. The employer's obligation changes with the needs of the system and the performance of the investments. In the case of the actuarial assumption, they look at how many people are working, how many people are -- what's the age profile for the workforce, how many people are nearing retirement, how much money is needed to meet the promises that have been made for these different variations on the pension things. And they come up with a number which, in many ways -- if you've read the ones -- the articles in the *New York Times* about the New York City systems -- these are numbers at a particular point that are used to give you a sense of where you are. And you have the valuation of your system, what your assets are. You have a number that is -- how much is our promise worth right now, and how close are we to meeting that?

So the short answer is, those calculations -- those actuarial calculations are made for each of the systems by the Division of Pensions and Benefits.

ASSEMBLYMAN GIBLIN: Well, I mean, getting back-- So we don't have to conform to any IRS regulations? I mean, how do we deal with the unfunded liability going forward? We hope that we can improve on our investments? Is the State under any obligation to make an annual contribution? I mean, I know that--

It seems to me, it behooves us to deal with this issue. I mean, it's not going away. It's only going to exacerbate it if we don't have some mechanism in place that, in the next budget, there is going to be a like amount put in the budget. Not that I'm looking forward to it. But how do you deal with this?

MR. KELLY: The short answer, I believe, is that the financial soundness of the pension systems is a legislative responsibility.

ASSEMBLYMAN GIBLIN: But trustees and the director of pensions -- they don't have any -- they don't have to be advocates, if they're not collecting enough money, to come before the Legislature--

MR. KELLY: Well, they're free to be--

ASSEMBLYMAN GIBLIN: --or, even in the case-- I'm not saying they should do it -- but sue us under this law.

MR. KELLY: Well, whether they advocate it or not, it's up to the Legislature to appropriate money. That's a responsibility conferred to the Legislature under the Constitution.

ASSEMBLYMAN GIBLIN: One other issue with some of these abuses that have been existing, that the media's done reporting on: This

issue of holding two public jobs. The way I understand your legal opinion, if somebody had a vested benefit as a result of those two positions, it would be foolish now to limit them to one, because, in fact, you'd be getting less contributions. Is that not accurate?

MR. KELLY: People in multiple public jobs do pay 5 percent of each of those salaries into the retirement system.

ASSEMBLYMAN GIBLIN: I know. But one of the proposals being mentioned is about limiting people to a position with the highest salary. So the point I'm trying to get at-- Say, hypothetically, I had two jobs, one for 75 and one for 50. That's a total of 125. I already had my three high years at the 125. To enact that now for existing employees would only be hurting the system, because you'll be getting less contributions on the second job, or none, right? I'm trying to understand this.

If you think about it slowly-- In other words, I eliminate contributions on the second job, that means less contributions for the plan. I mean, it seems to me like you have to deal with--

MR. KELLY: Well, it also means a reduced employer contribution and, potentially, a lower benefit upon retirement. We don't address multiple PERS memberships -- or multiple public employee pension memberships, directly, in the opinion. We were extrapolating from our finding that a detrimental alteration of somebody's benefits would violate the contracts clause of the Constitution. Trying to apply that to that situation is just more difficult. Frankly, I'm not sure if we can say for sure that that would (indiscernible) the problem.

ASSEMBLYMAN GIBLIN: What about the issue of some of these--

MR. KELLY: But the way, to avoid that problem-- The better way to address that might be to prevent dual -- multiple employ -- or prevent multiple employments, rather than--

ASSEMBLYMAN GIBLIN: I know. But the point I'm getting at is that if people have a benefit that they -- where over the last three years they had the multiple jobs -- you can't take it away from them, correct?

MR. KELLY: That's what we were saying would be-- Yes.

ASSEMBLYMAN GIBLIN: Okay. What about the issues of some of these negative reports that have been issued by the SCI regarding superintendents of schools, where they load everything on to their pension plan the last year or two? Can we do anything with that? In other words, what the interpretation of a salary is -- I mean, they've kind of stretched the point.

MR. KELLY: Okay. On the multiple memberships, the less risky way, in terms of litigation of addressing that, might be to prohibit people from holding more than one public job, rather than saying they can have multiple jobs but only one PERS membership.

ASSEMBLYMAN GIBLIN: Yes, but that's only going forward.

MR. KELLY: Right. But on -- with respect to the school superintendents--

MS. ESPENSHADE: The Division of Pensions and Benefits, in their regulations, has a fairly detailed description of what qualifies for compensation for calculation of pensions.

In the case of the superintendent of schools, if the compensation figure sent to the Division of Pensions matches a paycheck, and it's the reported compensation, then that would be what the contribution rate is. They're paying the 5 percent on that rate. The State, on behalf of TPA, is making the contribution.

If they -- it is obvious that they have cobbled things that are in a contract, then the Division of Pensions examines this and would say, "This is not the correct compensation figure for your calculation." However, if the compensation negotiated with a superintendent of schools, in the contract, says, "My compensation is this amount," and that's what the paycheck says, then it lines up with other compensation and paychecks.

ASSEMBLYMAN GIBLIN: How many auditors do you have in the retirement system?

MS. ESPENSHADE: We wouldn't know that information.

ASSEMBLYMAN GIBLIN: You don't know?

MS. ESPENSHADE: You might-- Tomorrow, the Director of the Division of Pensions and Benefits will be here, talking about the systems again. And he might be able to give you some information.

ASSEMBLYMAN GIBLIN: So if there is this big spike in somebody's salary -- say you have a red flag up -- somebody over 60, you start seeing a big spike in their salary-- Even if they say that's salary, then they collect it, right? I mean, that seems to be the drill.

MS. ESPENSHADE: Well, as I said, there are criteria that are looked at. But if the employer says this is the salary, then it meets the definition of *salary*.

ASSEMBLYMAN GIBLIN: Okay. I just want to get a little insight about how it works.

Thank you.

ASSEMBLYWOMAN POU: Thank you, Assemblyman.

I see hands going up.

Senator Gormley, followed by Senator Rice.

SENATOR GORMLEY: If -- and I don't know if they do this in other states -- an individual has a vested right of pension, it can't be touched. But assume there is a statute on the books that if the individual would like to transfer a -- would like to, in effect, transfer a portion of that benefit to health benefits-- Suppose the health benefits plan isn't as large as they might like. Suppose the State offered an option: you voluntarily want to give up a portion of your pension, you could get an enhanced health benefit benefit. As long as it was voluntary for the individual, would that be a possibility?

MS. ESPENSHADE: I'm not quite sure whether you mean that you would actually be taking pension money out of the pension system to transfer it, or are you talking -- speaking of counterbalancing -- in speaking about giving up and achieving things?

SENATOR GORMLEY: Either way. Suppose the individual entitled to the pension -- or they're retired -- let's say they're retired. And they decide that it would be more meaningful for them to have an enhanced health benefit; and they were given an option, totally up to them, that they could have an enhanced health benefit over what they're entitled to if they transfer or voluntarily move -- however you might state it. Suppose they transfer that over to the other system. Is something like that done in other

states? Or would there be a prohibition, as long as it's voluntary? I mean, they have a vested right. They're the only ones who can touch it. But suppose they say, "We would prefer to have a lower pension but enhanced health benefits." Would it be possible to structure something that way?

MR. KELLY: Isn't that called paying for health benefits out of your pension?

I don't think we have an example of that. It sounds rather unique. The things that we have encountered are situations where states offer, as an alternative to the traditional pension membership, membership -- or participation in a 401(k) type of plan. But I don't know that we have an example of any state creating something like that for -- you get better health benefits if you voluntarily agree to forego part of your pension.

SENATOR GORMLEY: I'm just exploring, because these are the types of things that are going to go on in negotiations. And I understand it's a vested right.

But let us assume we do what the Murphy report recommended, in terms of health benefits, and develop a safety-net base plan. And then someone decides that they want other options, and they would prefer to trade off against their pension. I'd just like-- Is that something that could be considered, because it's voluntary? That's all.

MR. KELLY: I think we simply don't know today, Senator. I think that's--

SENATOR GORMLEY: Well, I would appreciate your checking that out.

MR. KELLY: Sure.

SENATOR GORMLEY: Because I know there are a lot-- I mean, we appreciate all the effort you've given to this already.

MS. ESPENSHADE: I think when you mentioned voluntary -- when we were talking about a court looking at being adversely affected -- there being some weighing and examination of that -- you would not be talking about within a pension system. You're talking about, sort of, more of a whole global benefits package.

SENATOR GORMLEY: And what I'm saying is, this is up to the individual. This is not a mandate. Say, "Listen, this, in terms of my needs, would benefit me more if I could transfer from one to the other." And there might be certain circumstances where an enhanced health benefit plan -- because of the inability to buy coverage or get coverage in other areas that you might want -- or enhanced coverage -- it might be more economical for those individuals to take advantage of that. Would you look into potential -- on a voluntary basis, period. Because I'm trying to look at this dollar globally, between health and pension. Because it's all coming from the same dollar.

MS. ESPENSHADE: Probably the only insight we could give is the key word *voluntary*. And as I mentioned, in Michigan, where -- or some other states -- where they've even -- when you're just talking about choices between pension systems, you actually say, "You have two options, and you have a choice." And that probably is a key to developing this idea.

SENATOR GORMLEY: No, I'm talking absolutely voluntary, absolutely choice. But you put it all on the table. It is that common-- It is that dollar, because it all comes out of the same pot, or funding sources, from government. And you give the person the option not only to choose

their health plan, but determine how their equity is distributed between health and pension. But totally their choice.

I appreciate your--

MR. KELLY: We'll have to look into that, Senator.

SENATOR GORMLEY: Thank you.

ASSEMBLYWOMAN POU: Senator Rice.

SENATOR RICE: Yes.

I need to raise this for the record, because after 20 years I get tired of hearing it without having enough information. And I want to preface my remarks by saying that the working class people in New Jersey, like elsewhere, oftentimes have to work more than one job to make ends meet. If you're making \$18,000 or \$20,000 working in government, in a plan -- you're able to secure another job on your off time in another system in government that's legal, then I don't understand how we save money.

The point I'm making is that, if there are two positions available, and based on my qualifications I'm able to secure both of them, because someone wants me there-- If you remove me, and you hire someone else, you're still paying the pension.

And the reason I want to go on record with this is because I'm tired of the politics of my colleagues and others, in both parties over the years -- keep giving the press -- through the press, keep giving the public -- that it's a bad thing. I look at my colleagues. Some are attorneys, some are presidents of other organizations, some are educators. And that's how they drive their income. But for some reason, if you want to talk about -- this whole issue is talking about dual office holding, or something like that, then

we need to put that into perspective. And I can tell you, there is no substantial savings regardless. It may sound sexy, it may be good.

If we're talking about employees, like the ones out here who don't make a lot of money and may have to go into another system, like the board of education or someplace, then you may be doing some harm to families. It is our responsibility to help in any way we can.

So the question is: Can you tell me, how do we save money if a person is in a couple of systems? I don't know about a lot of people being in three or four systems, or five or six systems. There are some in two, there are some that may be in three. And those numbers probably aren't substantial, when it comes across the board, when you average them out and do the math. But can you tell me how we get a substantial savings if we keep talking about someone working two jobs? We don't talk about professionals -- big law firms and doing something else as lawyers, big doctors doing-- I don't know. How do we save? Because I'm tired of hearing this thing about, you don't work any more. My father raised me saying, "You work as many jobs as you legally can to make ends meet. Don't depend on anybody. If you don't have any skills, go get something else. If you have skills, and they're not paying you enough, get something else."

Can you tell me how the pensions are affected by an employee holding a couple of jobs in government, in this case, where their pensions come together?

MS. ESPENSHADE: It is the case, as you said, that each employee in each position pays the prescriptive part -- which we mentioned earlier would be 5 percent in PERS -- and their employer pays the

concomitant employer contribution. I believe the discussions about people holding multiple positions in multiple jobs, whether it is in more than one pension system or a single pension system, are not necessarily focused on -- that this has a cost to the system. The actual quantification--

ASSEMBLYWOMAN POU: Senator, perhaps--

SENATOR RICE: Yes, well, through the Chair--

ASSEMBLYWOMAN POU: Senator, just give me a second.

Perhaps some of these questions can be best directed to Mr. Beaver tomorrow, who can -- who may have some of the financial information.

Right now, we're really dealing with the legal parameters of what we can and cannot do. Perhaps-- And there's some incredibly important questions that have been raised by Senator Rice, as well as my colleague, Assemblyman Tom Giblin, that deal with the financial end of that. And I know that we're going to have the benefit of having Mr. Beaver here tomorrow, again. So perhaps some of these financial issues you may want to consider raising again tomorrow.

SENATOR RICE: Fine, Madam Chair. Staff can make a note to remind me on that issue. And I raised it because Assemblyman Giblin raised the issue of two jobs.

I've heard many of the 120 legislators raise it -- politically raise it. And they were really targeting elected officials. And that's for who wins, who loses. And I get tired of it, because it seems to be a jealousy issue more than an economic issue. And I don't want it to be a part of this Committee's discussion if there are no real savings in it. That's what I'm talking about.

ASSEMBLYWOMAN POU: I understand.

Thank you very much. We'll certainly, certainly discuss that tomorrow. I think those questions deserve an answer.

Thank you.

Are there any other questions from the members?

SENATOR GORMLEY: I just want to make a comment when it's over.

ASSEMBLYWOMAN POU: Senator, you have a comment you want to make?

SENATOR GORMLEY: If the witnesses are completed, I was going to say-- I don't have any--

ASSEMBLYWOMAN POU: Well, I want to make sure that-- Are there-- If there are no other questions, and before we ask our guests to leave, what's your comment, Senator?

SENATOR GORMLEY: Let them leave before I-- Believe me, it's not a question for them. I just want to -- in terms of future hearings, that's all.

Well, what I was going to say--

Turn your mike off, so I can--

ASSEMBLYWOMAN POU: Go ahead, it's on.

SENATOR GORMLEY: There we go.

What I was going to say is, it's apparent from the testimony that the area where we would be able to effectuate property tax is the health benefits side. And consequently, I know we have -- it would be too early for tomorrow. But we do have a hearing a week from Thursday. I know we are dealing with pensions. But because we have to look for that impact on

property taxes now, I would hope that a week from Thursday we could move on a parallel track -- I know we're going to spend some time on pensions -- but split the other half on dealing with the development of the safety-net base plan that was recommended by the Murphy Commission. Because if we're going to look at real dollar savings, that's where the negotiations are going to take place, because that's not where the -- it's where the vested rights aren't existing. And that's where we should be focused.

I know we could have-- In fact, our staff has already spent some time. And if there is need for a safety-net base plan, we could have it by this afternoon. And that could serve as the basis for review. And, also, we could ask the Governor's Office if it's worth talking about. Because we are dealing with a limited time frame. And it's obvious, from the testimony today, we can't do long-term changes to the pension system. But the immediate need -- the immediate negotiations focus is benefits. And that's not limited by what we did in 1997. And I would suggest we take up benefits next week, especially following the lead of the Murphy report.

Thank you.

ASSEMBLYWOMAN POU: Thank you very much for your comments.

I think one of the comments that Senator Scutari mentioned in his opening remarks was laying out the foundation or some of the steps that we were going to move in, and what direction, and some of those issues. We'd like to make sure that we continue that route to ensure that we have covered everything that we can within those particular areas.

We recognize and appreciate your comments. We will take them and move as best as we can. But I'm not so sure that we're going to be able to do that as early as next week. But certainly those are good points, and ones that we will certainly move forward at the right time for us to be able to do that.

ASSEMBLYMAN O'TOOLE: Chair.

ASSEMBLYWOMAN POU: Thank you for your comments.

Assemblyman Giblin, and then followed by Assemblyman O'Toole.

ASSEMBLYMAN GIBLIN: Just two quick items: One, with the Murphy report. Maybe the staff could find out the legal basis with some of those recommendations that they've developed. In fact, they had some counsel on board. And the other thing is trying to get a response from the Governor's Office about the OLS report. I know they had made some representations early on. I assume we'll be getting something like that.

ASSEMBLYWOMAN POU: Thank you.

Assemblyman O'Toole.

ASSEMBLYMAN O'TOOLE: Thanks, Chair.

I just want to comment on Senator Gormley's comments. I happen to agree that-- I mean, we are just about 30 days into this special session. And I know there's a certain process that takes hold here. And while there are differences of opinion, that certainly came out today, as to whether judicially or legislatively we can change nonforfeitable rights-- I mean, that is all left for the greater decision with the legislative body, or maybe before the Supreme Court. I think the parameters have been staked out in that regard.

But I think there is some consensus that there will be a higher yield of potential tax dollars on the medical components. So I really would think that we would expedite that process. And if we're going to be here next Thursday, I would love to -- whether we spend a half a day or a whole day next Thursday -- just talk about a portion of the medical component, because I don't want to wait until September or October. You know, September is literally a week away. And our time frame is really coming up on our heels. And I just think we have a lot of work to get done. And if we can just push ahead with the agenda, I'd be grateful.

ASSEMBLYWOMAN POU: I think we all agree with you, Assemblyman. And that's certainly what our desire will be.

If the opportunity certainly arises, where we have been able to properly satisfy all of the concerns and questions of the Committee, as well as the presenters that are in front of us, leading -- giving us the opportunity to get to that very next step as early as next week, we will be most happy to do that.

I agree that we want to be able to move as expeditiously as possible. But we also need to be careful to make sure that we're not overlooking anything, so that we can try to get as much information as we can, so that we can move forward to the next point.

But there is absolutely no disagreement here. I think we're all on the same page.

Thank you.

Senator Scutari, did you have any closing remarks at this time?

SENATOR SCUTARI: Just briefly. I mean, clearly, I agree with what Assemblyman O'Toole and Senator Gormley stated. But we do

want to finish this portion of our educational analysis regarding pensions, and then move on to considerations regarding health benefits. But if we can do that next Thursday, certainly-- If we can prepare the staff to start thinking about some of the questions that we're going to ask, so we can think about what types of end-proposals that we might consider-- But we don't want to miss anything on the pensions aspect of it, in terms of what we can and can't do. And, obviously, we received a lot of information today regarding that.

So the Assembly Chair and myself will discuss that and see if we can get that together for next Thursday -- at least maybe the second portion of the meeting, or something like that.

Thank you.

ASSEMBLYWOMAN POU: Thank you, Senator.

And thank you Mr. Kelly and--

ASSEMBLYMAN GIBLIN: Just one thing, Madam Chairwoman.

ASSEMBLYWOMAN POU: Oh, I'm sorry, yes.

ASSEMBLYMAN GIBLIN: Maybe Pennsylvania, New York -- I know this process is going to take a while. But could we get the directors, possibly, here to kind of--

ASSEMBLYWOMAN POU: The directors from where?

ASSEMBLYMAN GIBLIN: From pensions programs, from Pennsylvania and New York.

ASSEMBLYWOMAN POU: Okay.

ASSEMBLYMAN GIBLIN: Just to understand what they're doing in their states.

ASSEMBLYWOMAN POU: Thank you.

Once again, thank you so very much, Mr. Kelly and Ms. Espenshade, for your presentation here today.

I want to also make sure to thank all the members of the public.

Excuse me, ladies and gentlemen. I just want to thank the members of the public for being here with us as well. Thank you so much for your participation.

ASSEMBLYMAN GIBLIN: Thank you, Assemblywoman.

ASSEMBLYWOMAN POU: Meeting adjourned.

**(MEETING CONCLUDED)**