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February 6, 2003

Representative Tim Knopp  
Chairman  
House Committee on Public Employee Retirement System  
900 Court St. NE H-295  
Salem OR 97301

Re: PERS  
Our File No.: 5415-237

Dear Representative Knopp:

The purpose of this letter is to comment on some of the statements recently made by Bill Gary, representing local jurisdictions, in both written and oral testimony before this committee. Clearly Mr. Gary's position relies very heavily on Judge Lipscomb's recent decision. It is not my intent to re-argue the issues of the Lipscomb case as Mr. Gary and I will have more than ample opportunity to do that in the appellate courts. However, the limits of the issues that Judge Lipscomb considered may not have been obvious from Mr. Gary's testimony.

The Scope of the Lipscomb Decision

To a substantial degree the issues that this committee and the legislature will face regarding actuarial equivalency issues are very different from those which were addressed by Judge Lipscomb. PERS will move to a set of updated mortality factors, whether by legislative or PERS board action, or both. At numerous hearings before the PERS board and its subcommittees as well as before this legislative committee the PERS Coalition has stated that it does not object to the adoption of updated mortality factors. The issue that the legislature will face is how to transition from the old set of tables to a new set of tables without interfering with protected contract rights or alternatively threatening the qualified status of the plan under the Internal Revenue Code. This is precisely the issue which has been at the center of the PERS board consideration of this issue, which has consumed most of the last two years.

In contrast, Judge Lipscomb was asked to determine whether the board's adoption of the 1993 rule, and the continued adherence to that rule, which provides that no new actuarial factors will be utilized if they result in a lowering of benefits, was inconsistent with the PERS statute. Judge Lipscomb found that it was. However, Judge Lipscomb did not give any specific direction to the PERS board on how they are to go about transitioning from current rules to a new set of rules. Judge Lipscomb did use the phrase "full and immediate implementation," but it is doubtful that he used it in the same sense that Mr. Gary has used it before this committee. In fact in a recent post-trial hearing, when Assistant Attorney General Steve Bushong, representing PERS, asked Judge Lipscomb for clarification of what he meant by "full and immediate implementation," Judge Lipscomb's response was extremely equivocal, ending with the thought that he just wanted to convey to the PERS board his desire that they do the right thing.<sup>1</sup>

A second, related issue is the extent of Judge Lipscomb's determination of individual contract rights in the current litigation. Mr. Gary made the truly remarkable assertion that neither the intervenors nor the State had bothered to raise the issue of contract rights before Judge Lipscomb because of the weakness of those arguments, and that they were foreclosed from being raised on appeal. Nothing could be further from the truth. In fact, the question of individual contract rights was very specifically not determined by Judge Lipscomb in this litigation. In a hearing which took place many months before trial, Judge Lipscomb considered the question of whether it was necessary or advisable to convert the pending litigation into a class action. Ultimately Judge Lipscomb decided not to do so, based primarily on his determination that it was not necessary for him to resolve individual contract issues in this litigation.<sup>2</sup> Attached to this letter is a portion of the trial transcript which contains a discussion on that specific issue between the court and counsel. In response to a request from the judge, I reminded the judge of the limitations which he had imposed on the litigation. I pointed out that based on his prior rulings, individual contract issues would be initially addressed by the PERS board upon remand and would not be addressed in the pending litigation. Judge Lipscomb described my statement as "absolutely correct." The sole reason that individual contract issues were not argued before Judge Lipscomb was because he determined that they were beyond the scope of the issues which were before him. While Mr. Gary and I might disagree about the exact scope of Judge Lipscomb's order, the suggestion that both the intervenors and the State failed to preserve individual contract issues is without foundation.

#### The Internal Revenue Code

Mr. Gary specifically disclaimed any particular expertise in the Internal Revenue Code and I join in that disclaimer as I, too, claim no particular expertise in that area. However, Mr. Gary goes on to state that I may have misstated the impact of the Internal Revenue Code on PERS and the potential impact on the ability to amend actuarial factors. Presumably Mr. Gary

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<sup>1</sup>I do not as yet have a transcript of these remarks but it has been ordered and will be shared with the committee upon receipt.

<sup>2</sup>The transcript of this hearing has also been ordered and will be provided to the committee upon receipt.

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refers to my letter of January 9, 2003 to Yvette Elledge for the PERS board. Mr. Gary appears to have misunderstood the purpose of that letter. The letter itself states quite clearly (at page 3) that Internal Revenue Code §411 does not apply to public sector plans like PERS. The PERS board used the private sector concept of “accrued benefit” in their proposed rule on actuarial equivalencies. The purpose of the letter was to explore the meaning of the term “accrued benefit” as applied to PERS which required an analysis under both ERISA and Internal Revenue Code as they applied to private sector pension plans.<sup>3</sup>

#### Judge Solomon’s Decision

During Mr. Gary’s presentation he was asked to reconcile Judge Solomon’s 1978 decision requiring the use of male only actuarial tables with Judge Lipscomb’s more recent decision. There is, in fact, no conflict between those decisions as they addressed different issues. In 1978 Judge Solomon determined that the use of separate male and female actuarial tables was discriminatory and ordered the PERS board to use male only tables. Curiously Mr. Gary dismissed the importance of this order by describing it as a consent decree, though I know of no legal theory under which consent decrees, once incorporated into a permanent injunction, have any less effect than fully-litigated decrees. However it also appears that Mr. Gary may not be familiar with the full scope of the *Henderson* litigation because the question of whether PERS was in violation of discrimination statutes was fully litigated before Judge Solomon, who determined that the use of separate tables was discriminatory. While the case was on appeal to the Ninth Circuit the U.S. Supreme Court reached an identical conclusion in a similar plan and upon remand to the trial court the stipulated order and injunction was entered.

The issue of whether it was appropriate to continue the use of male only tables was specifically raised in the Lipscomb litigation, but as was noted in the prior material that I have provided to the committee, Mr. Gary’s expert conceded that the use of male only tables was, in his opinion, within the discretion of the PERS board. Not only did Judge Lipscomb note that this issue had been conceded, but he carefully phrased his opinion and his final judgment to avoid any decision on the use of male only tables. Judge Lipscomb specifically refers to the practice of using what he referred to as outdated mortality tables but makes no mention of whether it is appropriate to continue to use male only actuarial tables.

Mr. Gary speculates that it may be possible to have the Oregon federal district court withdraw their injunction or perhaps limit the application of that injunction. However, if the purpose of lifting the injunction were to permit the utilization of actuarial tables as Mr. Gary has proposed without any look back protection, it would deprive all current PERS participants of the

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<sup>3</sup>The full extent of my Internal Revenue Code analysis was in my prior letter to this committee dated January 28, 2003, in which I pointed out that Internal Revenue Code §411(a)(25), which does apply to public sector plans, requires that pension plans provide a pension benefit which is “definitely determinable.” I suggested that a pension plan which continually changes actuarial assumptions and applies the latest of those assumptions at the time of retirement is inconsistent with this Internal Revenue Code requirement.

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benefit of that injunction during the entire time it was in effect. It is highly unlikely that the court would not only withdraw its injunction but in effect nullify its impact for the last 25 years.

The most difficult issue that the legislature must address in dealing with actuarial factors is how to transition between the current factors and a new set of factors in a way which protects not only contract rights but preserves the qualified status of the PERS plan under the Internal Revenue Code. Judge Lipscomb's opinion will provide very little assistance to the legislature in executing that task.

I would be happy to answer any other questions that the committee may have.

Yours very truly,

Gregory A. Hartman

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Enclosure

cc: PERS Coalition  
Senator Tony Corcoran  
House Committee