



H.F. 1759
(Smith, by request)

S.F. 1181
(Rosen, by request)

Executive Summary of Commission Staff Materials

Affected Pension Plan(s): PERA
Relevant Provisions of Law: Minnesota Statutes, Section 353F.04, Subdivision 1
General Nature of Proposal: PERA Privatizations; Decreasing Deferred Annuity Augmentation Rates for New Privatizations
Date of Summary: January 27, 2012

Specific Proposed Changes

- Revises deferred annuity augmentation rates for new PERA privatizations covered by Chapter 353F and occurring in 2011 or later. If the privatization occurs in 2011, the deferred annuity will be augmented by 1% per year rather than by 4% to age 55 and 6% thereafter. If the privatization occurs in 2012 or later, no augmentation will apply.

Policy Issues Raised by the Proposed Legislation

1. Whether any change is needed. The Commission may wish to consider that given the drastic revisions in 2010 in deferred annuity augmentation rates for numerous plans other than those applicable to privatized employees, a proposal to revise deferred annuity augmentation in PERA's privatized plan seems justified.
2. Whether any deferred annuity augmentation differential should remain between privatized and terminated employees.
3. The failure of this proposal to fully address equity issues created by leaving privatizations out of legislation enacted in 2010.
4. The degree to which the PERA privatization chapter and MSRS privatization chapter should differ.
5. The inconsistency between the 6% interest rate paid on refunds under the PERA privatization chapter compared to the 4% interest now paid under most other plans.
6. The actuarial condition of PERA-General.
7. The savings that would accrue to PERA and the resulting impact of those savings on the fund.

Potential Amendments

H1759-1A revises the PERA privatization chapter refund provision to pay 4% interest after July 1, 2011, making it comparable to MSRS and PERA terminated employee refund treatment and comparable to the refund treatment under the MSRS privatization chapter. May be used alone or with any other potential amendment.

Alternatives for revising the proposed PERA privatization deferred annuity augmentation treatment:

H1759-2A extends the proposed deferred annuity treatment of new privatizations to also apply to all existing PERA privatizations.

H1759-3A applies to new PERA privatizations only, and would leave a 1% differential between the deferred annuity augmentation treatment of terminated employees and those who are privatized.

H1759-4A is similar to H1759-3A, except that it applies to all PERA privatizations.

Alternatives to make changes in the MSRS privatization chapter deferred annuity augmentation treatment:

H1759-5A revises the MSRS privatization chapter to provide deferred annuities augmentation treatment for any new MSRS privatization, comparable to that which applies to MSRS terminated employees.

H1759-6A revises the MSRS privatization chapter to provide deferred annuities augmentation treatment for any MSRS privatization, new or old, comparable that which applies to MSRS terminated employees.

H1759-7A is similar to the -4A amendment for PERA privatizations. Under this amendment, any existing or new MSRS privatization would have augmentation that is 1% greater than that provided to otherwise-terminated MSRS employees after December 31, 2011.



TO: Members of the Legislative Commission on Pensions and Retirement
FROM: Ed Burek, Deputy Director *EB*
RE: H.F. 1759 (Smith, by request); S.F. 1181 (Rosen, by request): PERA Privatizations;
Decreasing Deferred Annuity Augmentation Rates for New Privatizations
DATE: January 27, 2012

Summary of H.F. 1759 (Smith, by request); S.F. 1181 (Rosen, by request)

H.F. 1759 (Smith, by request); S.F. 1181 (Rosen, by request) revises deferred annuity augmentation rates for new Public Employees Retirement Association (PERA) privatizations covered by Chapter 353F and occurring in 2011 or later. If the privatization occurred in 2011, the deferred annuity will be augmented by 1% per year rather than 4% deferred annuities augmentation to age 55 and 6% thereafter. If the privatization occurs in 2012 or later, no augmentation will apply.

Background Information on Relevant Topics

The following attachments provide background information on topics relevant to the proposed legislation:

- **Attachment A:** Background information on PERA treatment of privatized employees; differences between terminated and privatized employees.
- **Attachment B:** Financial sustainability provisions contained in Laws 2010, Chapter 359.
- **Attachment C:** Background information on the 2010 Financial Sustainability Measures regarding deferred annuities augmentation.

Discussion and Analysis

When a PERA-covered employing unit is privatized, the employees no longer meet the public employee definition. The policy that has been most often followed is to not permit the employees to continue as active members of the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General). However, if legislation is enacted to add these employees to the inclusion provision in Minnesota Statutes, Chapter 353F, the privatized employees have certain benefits, such as deferred annuity augmentation rates, that differ from the typical treatment of terminated employees.

The bill revises the deferred annuity augmentation rates, but only for privatizations that occur in 2011 or later, to match the deferred annuity augmentation rates now applicable to PERA-covered employees who terminate service. The augmentation rates under the PERA privatization chapter have always exceeded that applicable to terminated employees in situations other than a privatization, but the differential has grown considerably due to 2010 legislation which reduced deferred annuity augmentation rates applicable to PERA deferred retirees and those of most other major pension plans, without taking any similar action regarding privatizations.

For new privatizations, the proposed treatment matches the reduced augmentation rates applicable to PERA terminated employees under Chapter 353, which were reduced due to Laws 2010, Chapter 359, Article 1, Section 42. However, the change under the 2010 legislation to terminated PERA employees also applied to those who were already in deferred status. In contrast, the PERA proposed change for privatizations applies only to new privatizations, not those in effect prior to 2011.

H.F. 1759 (Smith); S.F. 1181 (Rosen) raises a number of pension and related public policy issues for consideration and possible discussion by the Commission, including the following:

1. Need for Change. The issue is whether any change is needed. The Commission may wish to consider that given the drastic revisions enacted in 2010 in deferred annuity augmentation rates for numerous plans other than those applicable to privatized employees, a proposal to revise deferred annuity augmentation in PERA's privatized plan seems justified. Under current law, if privatized employees are added to the applicable privatization chapter, they are treated far more favorably than PERA terminated employees. The privatized employee is likely to retain employment although with a different employer, is eligible for whatever pension coverage the new employer provides, and has generous deferred annuity augmentation for the deferred PERA pension. In contrast, a PERA-covered employee who terminates or is terminated may have no immediate employment prospects and thus have no

pension coverage, and has noticeably inferior deferred annuity augmentation on the deferred PERA annuity compared to the privatized employee. Due to the 2010 legislation, if the PERA-covered employee is terminated after January 1, 2012, the employee he will have no deferred annuity augmentation at all.

2. Extent of Differential between PERA Terminated Employees and PERA Privatized Employees. The policy issue is the extent of the differences between treatment of terminated employees and privatized employees. Since the PERA privatized employee chapter was created in 1999, PERA privatized employees have had more generous deferred annuities augmentation. The differential grew considerably when drastic cuts were passed in 2010 for deferred annuity augmentation for terminated PERA employees while no changes were made in the corresponding PERA privatized employee chapter. The 2010 legislation also included reductions in the interest rate paid on refunds of employee contributions to a terminated employee. For terminated employees the refund interest rate was decreased from six percent to four percent. No corresponding change was made in refunds paid to privatized employees. It is unclear whether the difference in refund interest rate treatment between PERA privatizations and PERA-General is intended by PERA or reflects an error. PERA may have forgotten to include this change in the 2010 legislation.
3. Failure of Proposal to Fully Address Deferred Annuitant Equity Issues. The policy issue is the failure of this proposal to fully address equity issues created by leaving privatizations out of legislation enacted in 2010. In the 2010 legislation, the reductions in deferred annuity augmentation applied to those already in deferred status, as well as to those who later become deferred retirees. In contrast, this current proposal will only impact those who become privatized in the future. No reductions are included for existing privatizations, or for those groups PERA is proposing to add to the included list in the PERA privatized employee chapter through other legislation during the current legislative session. This different treatment for those already in deferred status seems difficult to justify. If one argues that it is wrong to now revise treatment for those already in deferred status because of what was stated in statute at the time the privatization occurred regarding their benefits, then the 2010 legislation was equally wrong when it revised deferred annuity augmentation for all the existing terminated PERA, MSRS, TRA, and DTRFA deferred annuitants. If PERA is concerned that including existing privatizations in the current proposal would lead to a lawsuit, no legal issues would be raised that were not already pertinent due to the 2010 legislation.
4. MSRS/PERA Equity and Consistency Issues. The Commission may wish to consider the degree to which the PERA privatization chapter and MSRS privatization chapter should differ. The Commission has generally followed a model of treating similar employees in a comparable fashion. However, that principle was largely abandoned in the 2010 financial stability pension legislation. The MSRS privatization chapter (Minnesota Statutes, Chapter 352F) was created when the Legislature accepted a model proposed by MSRS to address an MSRS privatization situation, when the University of Minnesota Hospitals, whose employees had been public employees covered by MSRS-General, was merged with Fairview Hospital and its clinics. The PERA privatization chapter (Minnesota Statutes, Chapter 353F) was created shortly thereafter to deal with PERA privatizations, and was virtually identical to the MSRS privatization chapter. These chapters remained quite similar over time. Given the proposed change to PERA's privatization chapter, differences in treatment will be created between the MSRS and PERA's privatization chapters.
5. Extent of Proposed Rate Change. The policy issue is whether any deferred annuity augmentation differential should remain between privatized and terminated employees. PERA is proposing to eliminate any difference in the deferred annuity augmentation treatment between PERA privatized employees and PERA terminated employees for any new PERA privatizations in 2011 or later. Historically there has been a difference between the two groups, with privatized employees having higher rates. If the Commission continues to feel that some differential is appropriate, the Commission might conclude there is adequate justification to amend the bill to continue with some differential in treatment, although not as drastic as the differential in current law.
6. Refund Interest Rate Issue. The issue is inconsistency between the 6% interest rate paid on refunds under the PERA privatization chapter compared to the 4% interest now paid under most other plans. The 2010 Financial Sustainability Measures legislation (Laws 2010, Ch. 359, Art. 1) decreased the interest rate paid on refunds from 6% to 4% in the Teachers Retirement Association (TRA), Duluth Teachers Retirement Fund Association (DTRFA), all MSRS plans including the MSRS privatization chapter, and all PERA plans except the PERA privatization chapter. Given the changes made in refund interest rate policy in all those plans, including the MSRS privatization chapter, it is unclear why the PERA privatization chapter should continue to pay 6% interest on refunds. The Commission may wish to hear brief testimony from PERA regarding this refund interest rate issue. If the

Commission wishes to revise that treatment to match the treatment now in effect for all these other plans, including the MSRS privatization chapter, there is an amendment attached to accomplish this.

7. PERA- General Actuarial Condition. The policy issue is the actuarial condition of PERA-General, as indicated by the most recent actuarial valuation:

PERA-General 2011		
<u>Membership</u>		
Active Members		139,952
Service Retirees		62,198
Disabilitants		2,334
Survivors		7,289
Deferred Retirees		45,325
Nonvested Former Members		<u>109,630</u>
Total Membership		366,728
<u>Funded Status</u>		
Accrued Liability		\$17,898,849,000
Current Assets		<u>\$13,455,753,000</u>
Unfunded Accrued Liability		\$4,443,096,000
Funding Ratio	75.18%	
<u>Financing Requirements</u>		
Covered Payroll		\$5,183,629,000
Benefits Payable		\$950,708,000
Normal Cost	6.65%	\$344,925,000
Administrative Expenses	<u>0.19%</u>	<u>\$9,849,000</u>
Normal Cost & Expense	6.84%	\$354,774,000
Normal Cost & Expense	6.84%	\$354,774,000
Amortization	<u>6.63%</u>	<u>\$343,675,000</u>
Total Requirements	13.47%	\$698,449,000
Employee Contributions	6.25%	\$323,996,000
Employer Contributions	7.25%	\$375,846,000
Employer Add'l Cont.	0.00%	\$0
Direct State Funding	0.00%	\$0
Other Govt. Funding	0.00%	\$0
Administrative Assessment	<u>0.00%</u>	<u>\$0</u>
Total Contributions	13.50%	\$699,842,000
Total Requirements	13.47%	\$698,449,000
Total Contributions	<u>13.50%</u>	<u>\$699,842,000</u>
Deficiency (Surplus)	(0.03%)	(\$1,393,000)

8. Savings Implication. Impact on PERA-General Fund. The issue is the savings that would accrue to PERA and the resulting impact of those savings on the fund. PERA may be able to provide some information on this matter.

Potential Amendments for Commission Consideration

H1759-1A applies to the PERA privatization chapter refund provision and can be used alone or with any later amendments. This amendment revises the PERA privatization chapter refund provision to pay 4% interest after July 1, 2011, making it comparable to MSRS and PERA terminated employee refund treatment (Sec. 352.22, Subd. 2; and 353.34, Subd. 2) and comparable to the refund treatment under the MSRS privatization chapter (Sec. 352F.07).

The following are alternatives for revising the proposed PERA privatization deferred annuity treatment:

H1759-2A revises the bill by extending the proposed deferred annuity treatment of new privatizations to also apply to all existing PERA privatizations. This is the same approach that PERA took in 2010 when it revised deferred annuities augmentation treatment for terminated PERA employees. Those changes had the effect of applying retroactively to all individuals who had terminated in the past and already were in deferred annuity status.

H1759-3A applies to new PERA privatizations only, and would leave a 1% differential between the deferred annuity augmentation treatment of terminated employees and those who are privatized. The Commission may prefer this amendment if it concludes that some differential should remain between deferred annuity augmentation rates for terminated employees and those applicable to privatized employees.

H1759-4A is similar to H1759-3A, except that it applies to all PERA privatizations. All existing and new PERA privatizations would have augmentation that is 1% greater than that provided to otherwise comparable terminated employees.

The following are alternatives to make changes in the MSRS privatization chapter deferred annuity augmentation treatment:

H1759-5A revises the MSRS privatization chapter to provide deferred annuities augmentation treatment in the MSRS privatization chapter for any new MSRS privatization, comparable to that which applies to MSRS terminated employees. In any MSRS privatization occurring after the effective date of the provision, the deferred annuity augmentation rate will be 2%. This differs from the PERA treatment because in last year's legislation, although MSRS and PERA both revised their treatment of deferred annuities for terminated employees, the revisions were not the same. PERA requested and received larger reductions than those made to the MSRS plans.

H1759-6A revises the MSRS privatization chapter to provide deferred annuities augmentation treatment in the MSRS privatization chapter for any MSRS privatization, new or old, comparable that which applies to MSRS terminated employees. This is similar to the treatment in H1759-2A above. By impacting both old and new privatizations, under this amendment employees under the University of Minnesota Hospital/Fairview merger would be treated like any other MSRS deferred annuitant regarding augmentation rates applicable after December 31, 2011. Augmentation rates would be revised from 5.5% per year through age 55 and 7.5% per year thereafter, to 2% per year until the effective date of retirement for each year occurring after December 31, 2011.

H1759-7A is similar to H1759-4A for PERA privatizations. Under this amendment, any existing or new MSRS privatization would have augmentation that is 1% greater than that provided to otherwise-terminated MSRS employees after December 31, 2011. Under MSRS general law as revised in 2010, the augmentation rate after December 31, 2011, is 2.0% per year compounded annually until the effective date of retirement. Under this amendment, the augmentation rate for any existing or new MSRS privatizations will be 3.0% per year compounded annually until the effective date of retirement.

Background Information on PERA Treatment of Privatized Employees; Differences between Terminated and Privatized Employees

When a PERA-covered employing unit is privatized, the employees no longer meet the public employee definition. The policy that has been followed is to not permit the employees to continue as active members of the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General). However, if legislation is enacted to add these employees to the inclusion provision under Minnesota Statutes, Chapter 353F, the privatized employees have certain benefits that differ from the typical treatment of terminated employees.

One justification for this treatment is that the privatized employees did not choose to leave public service and to end public retirement plan coverage. Their employee status changed from public to nonpublic due to an action by the employer (the transfer from public employer to nonprofit corporation or other nonpublic status), rather than by an exercise of free will by the employees.

Minnesota Statutes 2010, Chapter 353F, states that if a privatization is included under that chapter, those employees who are employed at the time of the transfer to the nonprofit corporation receive the following special coverage provisions:

1. Vested Benefit With Any Service Length. The normal three-year PERA vesting period is waived, so a privatized employee with less than three years of PERA-covered service would be entitled to receive a PERA retirement annuity, notwithstanding general law.
2. Rule of 90 Eligibility with Post-Privatization Service. For privatized employees with actual or potential long service who could have retired early with an unreduced retirement annuity from PERA under the Rule of 90 (where the combination of age and total service credit totals 90), the employee will be able to count future privatized service with the privatized facility for eligibility purposes, but not for benefit computation purposes.
3. Increased Deferred Annuity Augmentation Rate. For the period between the date of privatization and the date of eventual retirement, the privatized employee's deferred PERA retirement annuity will increase at the rate of 4.0 percent until age 55 and at the rate of 6.0 percent thereafter until the effective date of retirement.
4. Enhanced Refund Interest Rate. If a privatized employee wants a refund of employee contributions rather than an eventual annuity, that refund is paid with six percent interest. In contrast, the treatment provided under PERA-General law is to pay six percent interest to July 1, 2011, and four percent interest thereafter.

Current Law: Treatment Difference between Terminated and Privatized Employees

The difference in treatment between a PERA terminated employee and a PERA privatized employee can be substantial. Consider an employee who is age 55 when the employer is privatized, and the employee group is added to the PERA privatization chapter. That employee's PERA annuity is increased by six percent per year prior to receipt. If the computed PERA annuity at age 55 is \$1,000 per month, the monthly annuity will be \$1,791 per month if the person waits to age 65 to start drawing the annuity. In contrast, an identical person who is terminated rather than privatized has only a one percent augmentation rate and will receive \$1,105 per month at age 65. If that identical person were to terminate after January 1, 2012, no augmentation is used and the person would receive only \$1,000 per month at age 65. Because of the difference in deferred annuity augmentation treatment, the privatized employee will receive a benefit at retirement that is 79 percent greater than the comparable employee who terminates employment after January 1, 2012.

The same information can be used to show the size of the change in treatment between different groups of privatized employees, since what PERA is proposing is to have the same deferred annuities augmentation rates for 2011 and later privatizations as apply to PERA terminated employees who are not privatized. If a PERA privatization occurred in the 2006 through 2010 period, the privatized employee age 55 with a computed \$1,000 per month pension has six percent per year deferred annuity augmentation. Commencing receipt of the annuity at age 65, the annuity will be \$1,791 per month. In contrast, an identical person privatized in 2011 will have one percent augmentation and receive a \$1,105 annuity at age 65. If the privatization occurs in 2012 or later, the annuity is not augmented during the deferral period and that comparable person will receive \$1,000 per month annuity at age 65.

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**Comparison of MSRS, PERA, TRA, and First Class City Teacher Retirement Fund Association
Financial Sustainability Proposals**

**Financial Sustainability Provisions Contained in the Omnibus Retirement Bill
S.F. 2918, 4th Enrossment, Article 1 (Laws 2010, Chapter 359)**

	MSRS-General	MSRS-Correct.	State Patrol	Judges	Legislators	ESO	PERA-General	PERA-Correct.	PERA-P&F	TRA	DTRFA	SPTRFA
a. Contributions												
1. Member	--	--	+2.0%	--	--	--	+0.25%	--	+0.2%	+2.0%	+1.00%	+1.00% Coord; +1.00% Basic
2. Employer	--	--	+3.0%	--	--	--	+0.25%	--	+0.3%	+2.0%	+1.00%	+1.00% C&B
3. Contribution rate stabilizer	--	--	--	--	--	--	Modified	--	--	Added	--	--
b. Post-retirement adjustments	Reduced from 2.5% to 2.0%, restored when 90% funded on MVB;* 6-mo. waiting period imposed for initial increase	Reduced from 2.5% to 2.0%, restored when 90% funded on MVB;* 6-mo. waiting period imposed for initial increase	Reduced from 2.5% to 1.5%, restored when 90% funded on MVB;* 6-mo. waiting period imposed for initial increase	Reduced from 2.5% to 2.0%, restored when 90% funded on MVB;* 6-mo. waiting period imposed for initial increase	Reduced from 2.5% to 2.0%, restored once MSRS-General is 90% funded on MVB;* 6-mo. waiting period for initial increase	Reduced from 2.5% to 2.0%, restored once MSRS-General is 90% funded on MVB;* 6-mo. waiting period for initial increase	Reduced from 2.5% to 1.0%, restored when 90% funded on MVB,* rate reduced if fund later declines from 90% funded	Reduced from 2.5% to 1.0%, restored when 90% funded on MVB,* rate reduced if fund later declines from 90% funded	Reduced from 2.5% to 1.0% for 1/1/2011 and 1/1/2012, then equal to the CPI percentage for the preceding fiscal year, not to exceed 1.5% until 90% funded on MVB,* then not to exceed 2.5%, but rate reduced if fund later declines from 90% funded	Suspended for 1/1/2011 & 1/1/2012; starting 1/1/2013, reduced from 2.5% to 2.0%, restored when 90% funded on MVB;* 6-mo. waiting period for initial increase	0% when less than 80% funded on MVB,* 1% when 80%-90% funded on MVB,* and 2% when more than 90% funded on MVB;* when 90% funded on AVB** moves to inflation match up to 5%	Suspended for 1/1/2011
c. Interest on refunds	Reduced from 6% to 4% after 6/30/2011	Reduced from 6% to 4% after 6/30/2011	Reduced from 6% to 4% after 6/30/2011	Reduced from 6% to 4% after 6/30/2011	Reduced from 6% to 4% after 6/30/2011	--	Reduced from 6% to 4% after 6/30/2011	Reduced from 6% to 4% after 6/30/2011	Reduced from 6% to 4% after 6/30/2011	Reduced from 6% to 4% after 6/30/2011	Reduced from 6% to 4% after 6/30/2010	--
d. Deferred annuities augmentation	Reduced from 5, 3, or 2.5% to 2% after 12/31/2011	Reduced from 5, 3, or 2.5% to 2% after 12/31/2011	Reduced from 5, 3, or 2.5% to 2% after 12/31/2011	--	Reduced from 5, 3, or 2.5% to 2% after 12/31/2011	--	Reduced from 5, 3, or 2.5% to 1% for plan members terminating before 1/1/2012, and eliminated for plan members terminating after 12/31/2011	Reduced from 5, 3, or 2.5% to 1% for plan members terminating before 1/1/2012, and eliminated for plan members terminating after 12/31/2011	Reduced from 5, 3, or 2.5% to 1% for plan members terminating before 1/1/2012, and eliminated for plan members terminating after 12/31/2011	Reduced from 5, 3, or 2.5% to 2% after 6/30/2012	Reduced from 5, 3, or 2.5% to 2% after 7/1/2012	--
e. Reemployed annuitant earnings limitation deferral account interest	Eliminated after 1/1/2011	Eliminated after 1/1/2011	--	--	--	--	Eliminated after 1/1/2011	Eliminated after 1/1/2011	Eliminated after 1/1/2011	Eliminated after 1/1/2011	Eliminated after 6/30/2010	--
f. Vesting service requirement	For new members after 6/30/2010, increased from 3 years to 5 years	For new members after 6/30/2010, increased from 3 years to 50% vested w/5 years-100% w/10 years	For new members after 6/30/2010, increased from 3 years to 5 years	--	--	--	For new members after 6/30/2010, increased from 3 years to 5 years	For new members after 6/30/2010, increased from 3 years to 50% vested w/5 years-100% w/10 years	For new members after 6/30/2010, incr. from 3 yrs to 50% vested w/ 5 yrs-100% w/10 yrs	--	For new members after 6/30/2010, increased from 3 years to 5 years	--
g. Early retirement reduction factor, per year under age 55	--	For pre-6/30/2010 members retiring after 6/30/2015 and for new members after 6/30/2010, increased from 2.4% to 5.0%	For new members after 6/30/2010, increased from 1.2% to 2.4%	--	--	--	--	--	--	--	--	--
h. Benefit accrual rate percentage, per year of high-5 average salary	--	For new members after 6/30/2010, reduced from 2.4% to 2.2%	--	--	--	--	--	--	--	--	--	--

*MVB = Market Value Basis

**AVB = Actuarial Value Basis

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Background Information on 2010 Financial Sustainability Measures Regarding Deferred Annuities Augmentation

The funding status of all defined benefit plans was considerably impacted by the market crash of 2008 and early 2009, which accompanied the major economic downturn that has been called the Great Recession. This caused a considerable decrease in funding ratios (assets divided by liabilities) for Minnesota pension plans because of the fall in pension plan asset values, and an increase in unfunded liabilities (the amount by which liabilities exceed assets). To address this situation, the 2010 Legislature passed legislation recommended by the executive directors of PERA, the Minnesota State Retirement System (MSRS), the Teachers Retirement Association (TRA), and the Duluth Teachers Retirement Fund Association (DTRFA). That legislation, enacted as Laws 2010, Chapter 359, Article 1, entitled Financial Sustainability Measures, included contribution rate increases for some Minnesota public plans, generally to be phased in over several years, and proposed changes in plan benefits to reign in liabilities. These changes included:

- contribution rate increases for some plans;
- reductions in the amount of increase after retirement for all plans, including temporary suspensions of any increase in TRA and DTRFA;
- reduced interest on refunds;
- reductions in deferred annuity augmentation;
- elimination of interest payments on reemployed annuitant savings accounts;
- increased vesting requirements for several plans;
- less generous early retirement reduction factors for the Correctional Employees Retirement Plan of the Minnesota State Retirement System (MSRS-Correctional) and the State Patrol Retirement Plan; and
- a lower benefit accrual rate for MSRS-Correctional.

The St. Paul Teachers Retirement Fund Association (SPTRFA) chose not to be included in these broad changes, except for a one-year suspension in its cost of living adjustment for its retirees.

The changes in PERA and MSRS system plans described above did not include the MSRS privatized employee chapter, Minnesota Statutes, Chapter 352F, nor did it include the PERA privatized employee chapter, Minnesota Statutes, Chapter 353F.

The particular 2010 change relevant for understanding the implications of the current bill is the treatment of deferred annuities augmentation. Attachment A indicates the revisions to the deferred annuities augmentation provisions across the various plans. (The SPTRFA does have a deferred annuities augmentation provision, but chose not to revise its rates. The closed Legislators Plan and the closed Elected State Officers plan, which covered constitutional officers, do not have deferred annuities augmentation provisions. All other plans—the remainder of the MSRS system plans and PERA plans other than privatization chapters, TRA, and the DTRFA—revised their provisions.) As is shown in that table, the revisions in deferred annuities augmentation provisions varied in amount and in change dates across plan systems, with reductions in PERA plans being the most severe. For PERA plans the reduction was from 5, 3, or 2.5 percent annual augmentation (the applicable rate varied based on age and whether the person terminated service before or after 2006) to 1.0 percent for plan members terminating before 2012, and no augmentation for those terminating on or after January 1, 2011.

The 2010 changes were significant not only for the amount of the changes, but for the nature of the changes. The changes in post-retirement adjustments applied to those already retired as well as new retirees. The reductions in deferred annuity augmentation rates applied to current employees when they terminate service and enter deferred annuitant status, and also to those already in deferred status. Thus these changes violated the general concept of an implied contract, that the applicable law governing a person's pension is the law in effect when the person terminated covered employment.

The 2010 legislative reductions in post-retirement adjustments have been challenged in court, although it may be a few years before that process is complete. No lawsuit has been filed regarding the deferred annuity augmentation rate changes, although the issues are similar and the reductions more severe. The previous time that deferred annuity augmentation rates were revised for these pension plans was in 2006 (Laws 2006, Ch. 277, Art. 2). Those changes, however, were for new hires only, thus avoiding any implied contract issues. The 2006 Legislature also revised deferred annuity augmentation rates under privatizations (Laws 2006, Ch. 27, Art. 5), creating the rates now applicable to post-2006 privatizations (four percent to age 55 and six percent thereafter). Again, by making the changes applicable only to new privatizations, those changes largely avoided implied contract issues.

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MSRS refund treatment:

352F.07 EFFECT ON REFUND.

Notwithstanding any provision of chapter 352 to the contrary, terminated hospital employees may receive a refund of employee accumulated contributions plus interest in accordance with section 352.22, subdivision 2, at any time after the transfer of employment to Fairview, University of Minnesota Physicians, or University Affiliated Family Physicians. If a terminated hospital employee has received a refund from a pension plan enumerated in section 356.30, subdivision 3, the person may not repay that refund unless the person again becomes a member of one of those enumerated plans and complies with section 356.30, subdivision 2.

PERA refund treatment:

353F.07 EFFECT ON REFUND.

Notwithstanding any provision of chapter 353 to the contrary, terminated medical facility or other public employing unit employees may receive a refund of employee accumulated contributions plus interest at the rate of six percent per year compounded annually in accordance with section 353.34, subdivision 2, of the edition of Minnesota Statutes published in the year in which the privatization occurred, at any time after the transfer of employment to the successor employer to the medical facility or other public employing unit. If a terminated medical facility employee has received a refund from a pension plan enumerated in section 356.30, subdivision 3, the person may not repay that refund unless the person again becomes a member of one of those enumerated plans and complies with section 356.30, subdivision 2.

MSRS terminated employee refunds:

352.22 REFUND OR DEFERRED ANNUITIES.

Subd. 2. Amount of refund. Except as provided in subdivision 3, the refund payable to a person who ceased to be a state employee by reason of a termination of state service is an amount equal to employee accumulated contributions plus interest at the rate of six percent per year compounded daily from the date that the contribution was made until June 30, 2011, or until the date on which the refund is paid, whichever is earlier, and at the rate of four percent per year compounded daily from the date that the contribution was made or from July 1, 2011, whichever is later, until the date on which the refund is paid. Included with the refund is any interest paid as part of repayment of a past refund, plus interest thereon from the date of repayment.

PERA terminated employee refunds:

353.34 RIGHTS UPON TERMINATION OF MEMBERSHIP.

Subd. 2. Refund with interest. (a) Except as provided in subdivision 1, any person who ceases to be a public employee is entitled to receive a refund in an amount equal to accumulated deductions with annual compound interest to the first day of the month in which the refund is processed.

(b) For a person who ceases to be a public employee before July 1, 2011, the refund interest is at the rate of six percent to June 30, 2011, and at the rate of four percent after June 30, 2011. For a person who ceases to be a public employee after July 1, 2011, the refund interest is at the rate of four percent.

(c) If a person repays a refund and subsequently applies for another refund, the repayment amount, including interest, is added to the fiscal year balance in which the repayment was made.

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1.1 moves to amend H.F. No. 1759; S.F. No. 1181 as follows:

1.2 Page 2, after line 21, insert:

1.3 "Sec. 2. Minnesota Statutes 2010, section 353F.07, is amended to read:

1.4 **353F.07 EFFECT ON REFUND.**

1.5 Notwithstanding any provision of chapter 353 to the contrary, terminated medical
1.6 facility or other public employing unit employees may receive a refund of employee
1.7 accumulated contributions plus interest ~~at the rate of six percent per year compounded~~
1.8 ~~annually as provided in accordance with~~ section 353.34, subdivision 2, ~~of the edition~~
1.9 ~~of Minnesota Statutes published in the year in which the privatization occurred;~~ at any
1.10 time after the transfer of employment to the successor employer ~~to~~ of the terminated
1.11 medical facility or other public employing unit. If a terminated medical facility or other
1.12 public employing unit employee has received a refund from a pension plan ~~enumerated~~
1.13 listed in section 356.30, subdivision 3, the person may not repay that refund unless the
1.14 person again becomes a member of one of those ~~enumerated~~ listed plans and complies
1.15 with section 356.30, subdivision 2.

1.16 **EFFECTIVE DATE.** This section is effective the day following final enactment."

1.17 Amend the title accordingly

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1.1 moves to amend H.F. No. 1759; S.F. No. 1181 as follows:

1.2 Page 1, after line 5, insert:

1.3 "Section 1. Minnesota Statutes 2010, section 353.71, subdivision 2, is amended to read:

1.4 Subd. 2. **Deferred annuity computation; augmentation.** (a) The deferred annuity
1.5 accruing under subdivision 1, or under sections 353.34, subdivision 3, ~~and~~ 353.68,
1.6 subdivision 4, and 353F.04, subdivision 1, must be computed on the basis of allowable
1.7 service prior to the termination of public service and augmented as provided in this
1.8 subdivision. The required reserves applicable to a deferred annuity, or to any deferred
1.9 segment of an annuity, must be determined as of the first day of the month following the
1.10 month in which the former member ceased to be a public employee, or July 1, 1971,
1.11 whichever is later.

1.12 (b) For a person who became a public employee before July 1, 2006, whose period
1.13 of deferral began after June 30, 1971, and who terminated public employment before
1.14 January 1, 2012, the required reserves of the deferred annuity must be augmented at the
1.15 following applicable rate or rates:

1.16 (1) five percent annual compound interest until January 1, 1981;

1.17 (2) three percent annual compound interest after January 1, 1981, or until the
1.18 earlier of December 31, 2011, or after the date of the termination of public service or the
1.19 termination of membership, whichever is later, until January 1 of the year following the
1.20 year in which the former member attains age 55;

1.21 (3) five percent annual compound interest from January 1 of the year following the
1.22 year in which the former member attains age 55, or until December 31, 2011, whichever
1.23 is earlier; and

1.24 (4) one percent annual compound interest from January 1, 2012.

1.25 (c) For a person who became a public employee after June 30, 2006, and who
1.26 terminated public employment before January 1, 2012, the required reserves of the
1.27 deferred annuity must be augmented at 2.5 percent annual compound interest from the date

2.1 of termination of public service or termination of membership, whichever is earlier, until
 2.2 December 31, 2011, and one percent annual compound interest after December 31, 2011.

2.3 (d) For a person who terminates public employment after December 31, 2011, the
 2.4 required reserves of the deferred annuity must not be augmented.

2.5 (e) If a person has more than one period of uninterrupted service, the required
 2.6 reserves related to each period must be augmented as specified in this paragraph. The sum
 2.7 of the augmented required reserves is the present value of the annuity. Uninterrupted
 2.8 service for the purpose of this subdivision means periods of covered employment during
 2.9 which the employee has not been separated from public service for more than two years.
 2.10 If a person repays a refund, the restored service must be considered as continuous with the
 2.11 next period of service for which the employee has credit with this association. This section
 2.12 must not reduce the annuity otherwise payable under this chapter. This paragraph applies
 2.13 to individuals who become deferred annuitants on or after July 1, 1971. For a member
 2.14 who became a deferred annuitant before July 1, 1971, the paragraph applies from July 1,
 2.15 1971, if the former active member applies for an annuity after July 1, 1973.

2.16 (f) The retirement annuity or disability benefit of, or the survivor benefit payable
 2.17 on behalf of, a former member who terminated service before July 1, 1997, or the
 2.18 survivor benefit payable on behalf of a basic or police and fire member who was receiving
 2.19 disability benefits before July 1, 1997, which is first payable after June 30, 1997, must
 2.20 be increased on an actuarial equivalent basis to reflect the change in the postretirement
 2.21 interest rate actuarial assumption under section 356.215, subdivision 8, from five percent
 2.22 to six percent under a calculation procedure and tables adopted by the board and approved
 2.23 by the actuary retained under section 356.214.

2.24 **EFFECTIVE DATE.** This section is effective the day following final enactment."

2.25 Page 1, line 7, strike "Enhanced" and before "The" insert "Section 353.71,
 2.26 subdivision 2, applies to"

2.27 Page 1, line 8, strike " is subject" and insert " _"

2.28 Page 1, lines 9 to 24, delete the new language and strike the old language

2.29 Page 2, delete lines 1 to 20

2.30 Renumber the sections in sequence

2.31 Amend the title accordingly

- 1.1 moves to amend H.F. No. 1759; S.F. No. 1181 as follows:
- 1.2 Page 2, line 4, delete "3.0" and insert "4.0"
- 1.3 Page 2, line 7, delete "5.0" and insert "6.0"
- 1.4 Page 2, line 9, delete "1.0" and insert "2.0"
- 1.5 Page 2, line 13, delete "2.5" and insert "3.5"
- 1.6 Page 2, line 15, delete "1.0" and insert "2.0"
- 1.7 Page 2, line 17, delete "no"
- 1.8 Page 2, line 18, delete "augmentation applies" and insert "the augmentation rate is
- 1.9 1.0 percent compounded annually until the effective date of retirement"

1.1 moves to amend H.F. No. 1759; S.F. No. 1181 as follows:

1.2 Page 1, line 7, strike "Enhanced" and before "The" insert "Section 353.71,
1.3 subdivision 2, applies to"

1.4 Page 1, line 8, strike "is subject" and insert "except that one percent must be added
1.5 to the augmentation rate or rates otherwise applicable as stated in that subdivision. If no
1.6 augmentation would be provided under that subdivision, augmentation of one percent
1.7 compounded annually until the effective date of retirement must be applied."

1.8 Page 1, lines 9 to 24, delete the new language and strike the old language

1.9 Page 2, delete lines 1 to 20

1.10 Amend the title accordingly

1.1 moves to amend H.F. No. 1759; S.F. No. 1181 as follows:

1.2 Page 1, after line 5, insert:

1.3 "Section 1. Minnesota Statutes 2010, section 352F.04, subdivision 1, is amended to
1.4 read:

1.5 Subdivision 1. **Enhanced augmentation rates.** (a) The deferred annuity of a
1.6 terminated hospital employee who attained that status before June 2, 2006, is subject to
1.7 augmentation under Minnesota Statutes 1994, section 352.72, subdivision 2, except that
1.8 the rate of augmentation is 5.5 percent compounded annually until January 1 following the
1.9 year in which the person attains age 55. From that date to the effective date of retirement,
1.10 the augmentation rate is 7.5 percent compounded annually.

1.11 (b) If a terminated hospital employee attained that status ~~on or~~ after June ~~2~~ 1, 2006,
1.12 and before January 1, 2012, the augmentation rate is four percent compounded annually
1.13 until January 1, following the year in which the person attains age 55. From that date to
1.14 the effective date of retirement, the augmentation rate is six percent compounded annually.

1.15 (c) If a terminated hospital employee attained that status after December 31, 2011,
1.16 the augmentation rate is two percent compounded annually until the effective date of
1.17 retirement.

1.18 **EFFECTIVE DATE.** This section is effective the day following final enactment."

1.19 Renumber the sections in sequence

1.20 Amend the title accordingly

1.1 moves to amend H.F. No. 1759; S.F. No. 1181 as follows:

1.2 Page 1, after line 5, insert:

1.3 "Section 1. Minnesota Statutes 2010, section 352F.04, subdivision 1, is amended to
1.4 read:

1.5 Subdivision 1. **Enhanced augmentation rates.** (a) Except as otherwise specified in
1.6 paragraph (c) for periods after December 31, 2011, the deferred annuity of a terminated
1.7 hospital employee who attained that status before June 2, 2006, is subject to augmentation
1.8 under Minnesota Statutes 1994, section 352.72, subdivision 2, except that the rate of
1.9 augmentation is 5.5 percent compounded annually until January 1 following the year in
1.10 which the person attains age 55. From that date to the effective date of retirement, the
1.11 augmentation rate is 7.5 percent compounded annually.

1.12 (b) Except as otherwise specified in paragraph (c) for periods after December 31,
1.13 2011, if a terminated hospital employee attained that status on or after June 2, 2006, the
1.14 augmentation rate is four percent compounded annually until January 1, following the
1.15 year in which the person attains age 55. From that date to the effective date of retirement,
1.16 the augmentation rate is six percent compounded annually.

1.17 (c) Notwithstanding paragraphs (a) and (b), after December 31, 2011, the
1.18 augmentation rate is 2.0 percent compounded annually until the effective date of
1.19 retirement.

1.20 **EFFECTIVE DATE.** This section is effective the day following final enactment."

1.21 Renumber the sections in sequence.

1.22 Amend the title accordingly

1.1 moves to amend H.F. No. 1759; S.F. No. 1181 as follows:

1.2 Page 1, after line 5, insert:

1.3 "Section 1. Minnesota Statutes 2010, section 352F.04, subdivision 1, is amended to
1.4 read:

1.5 Subdivision 1. **Enhanced augmentation rates.** (a) Except as otherwise specified in
1.6 paragraph (c) for periods after December 31, 2011, the deferred annuity of a terminated
1.7 hospital employee who attained that status before June 2, 2006, is subject to augmentation
1.8 under Minnesota Statutes 1994, section 352.72, subdivision 2, except that the rate of
1.9 augmentation is 5.5 percent compounded annually until January 1 following the year in
1.10 which the person attains age 55. From that date to the effective date of retirement, the
1.11 augmentation rate is 7.5 percent compounded annually.

1.12 (b) Except as otherwise specified in paragraph (c) for periods after December 31,
1.13 2011, if a terminated hospital employee attained that status on or after June 2, 2006, the
1.14 augmentation rate is four percent compounded annually until January 1, following the
1.15 year in which the person attains age 55. From that date to the effective date of retirement,
1.16 the augmentation rate is six percent compounded annually.

1.17 (c) Notwithstanding paragraphs (a) and (b), after December 31, 2011, the
1.18 augmentation rate is 3.0 percent compounded annually until the effective date of
1.19 retirement.

1.20 **EFFECTIVE DATE.** This section is effective the day following final enactment."

1.21 Renumber the sections in sequence.

1.22 Amend the title accordingly

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State of Minnesota
HOUSE OF REPRESENTATIVES

EIGHTY-SEVENTH
SESSION

HOUSE FILE No. **1759**

May 22, 2011

Authored by Smith and by request

The bill was read for the first time and referred to the Committee on Government Operations and Elections

1.1 A bill for an act
1.2 relating to retirement; Public Employees Retirement Association privatizations;
1.3 decreasing augmentation rates applicable to new privatizations; amending
1.4 Minnesota Statutes 2010, section 353F.04, subdivision 1.

1.5 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MINNESOTA:

1.6 Section 1. Minnesota Statutes 2010, section 353F.04, subdivision 1, is amended to read:

1.7 Subdivision 1. **Enhanced augmentation rates.** (a) The deferred annuity of
1.8 a terminated medical facility or other public employing unit employee is subject
1.9 to augmentation under section 353.71, subdivision 2, of the edition of Minnesota
1.10 Statutes published in the year in which the privatization occurred, except that the rate
1.11 of augmentation is as specified in ~~paragraph (b) or (c), whichever is applicable~~ this
1.12 subdivision.

1.13 (b) This paragraph applies if the legislation adding the medical facility or other
1.14 employing unit to section 353F.02, subdivision 4 or 5, as applicable, was enacted before
1.15 July 26, 2005, and became effective before January 1, 2008, for the Hutchinson Area
1.16 Health Care or before January 1, 2007, for all other medical facilities and all other
1.17 employing units. For a terminated medical facility or other public employing unit
1.18 employee, the augmentation rate is 5.5 percent compounded annually until January 1
1.19 following the year in which the person attains age 55. From that date to the effective date
1.20 of retirement, the augmentation rate is 7.5 percent compounded annually.

1.21 (c) If paragraph (b) is not applicable, and if the effective date of the privatization is
1.22 before January 1, 2011, the augmentation rate is four percent compounded annually until
1.23 January 1, following the year in which the person attains age 55. From that date to the
1.24 effective date of retirement, the augmentation rate is six percent compounded annually.

- 2.1 (d) If the effective date of the privatization is after December 31, 2010, and before
2.2 January 1, 2012, and if the person became a public employee on or before June 30, 2006:
- 2.3 (1) if the former member is less than age 55 on January 1, 2011, the augmentation
2.4 rate is at a 3.0 percent annual rate through December 31, 2011, prorated if the privatization
2.5 occurs less than one full year before January 1, 2012;
- 2.6 (2) if the former member is age 55 or older on January 1, 2011, the augmentation
2.7 rate is at a 5.0 percent annual rate through December 31, 2011, prorated if the privatization
2.8 occurs less than one full year before January 1, 2012; and
- 2.9 (3) regardless of age, after December 31, 2011, the augmentation rate is 1.0 percent
2.10 compounded annually until the effective date of retirement.
- 2.11 (e) If the effective date of the privatization is after December 31, 2010, and before
2.12 January 1, 2012, and if the person became a public employee after June 30, 2006:
- 2.13 (1) the augmentation rate is at a 2.5 percent annual rate through December 31, 2011,
2.14 prorated if the privatization occurs less than one year before January 1, 2012; and
- 2.15 (2) after December 31, 2011, the augmentation rate is 1.0 percent compounded
2.16 annually until the effective date of retirement.
- 2.17 (f) If the effective date of the privatization is January 1, 2012, or later, no
2.18 augmentation applies.
- 2.19 (g) The term "effective date of the privatization" as used in this subdivision means
2.20 the "effective date" as defined in section 353F.02, subdivision 3.
- 2.21 **EFFECTIVE DATE.** This section is effective the day following final enactment.