January 23, 1998
Room 318, Capitol

17th Meeting

LEGISLATIVE COMMISSION ON PENSIONS AND RETIREMENT

MINUTES

Senator Steven Morse, Chair of the Legislative Commission on Pensions and Retirement, called the meeting to order at 2:15 P.M.

Commission members present:
Representatives Mike Delmont, Richard Jefferson, Phyllis Kahn, Harry Mares, and Mary Murphy
Senators Don Betzold, Dean Johnson, Steven Morse, Lawrence Pogemiller, and Roy Terwilliger

Commission members absent:
Representative Steve Smith and Senator LeRoy Stumpf

Agenda Items Discussed

1. **Review of the 1997 Actuarial Valuations of the Statewide and Major Public Pension Plans by Mr. Thomas Custis, FSA, Milliman & Robertson, Inc.**
Mr. Thomas Custis, Milliman & Robertson, Inc., began his overview of the Summary of 1997 Actuarial Valuations. He stated that major changes occurred in 1997 including benefit changes provided by the uniformity law, assumption changes for many plans including the first class city teacher plans, and favorable asset experience due to high investment returns. He referred members to the colored charts in the booklets provided by Milliman & Robertson, Inc. Mr. Custis testified that PERA shows a modest deficiency, PERA-P&F shows a considerable sufficiency, and MSRS shows a sufficiency. For MSRS-Correctional, the actuarial contribution requirement for normal cost and expenses increased because of modest losses due in part to expanded membership and assumption changes. However, a statutory change in the uniformity bill allowed the Correctional Plan to recognize its negative unfunded liability, which means on a current actuarial basis they are overfunded, so the MSRS-Correctional Plan shows a sufficiency. Rep. Murphy asked what would happen if an additional 100 people were added to the Correctional Plan. Mr. Custis stated that if they were new employees, there would not be an impact on the current funded level but it might raise the normal cost slightly. Mr. Custis continued his review and stated that the State Patrol shows a sufficiency as does the Judges Plan. Sen. Morse noted that the judges employee contribution is disproportionately low compared to other employee contributions and it is very visually represented in this table. Mr. Custis went on to state that TRA shows a dramatic sufficiency so, as prescribed in statutes, the employer additional contribution will be eliminated. He stated that DTRFA is showing a deficiency, while MTRFA has a slight sufficiency due to the significant direct state aid provided in the uniformity bill. StPTRFA was provided the largest benefit increase under the uniformity bill but is showing a slight sufficiency because of the significant direct state aid they also received in the uniformity bill. Representative Mares asked what was included in supplemental costs. Mr. Custis stated that the liability for the plan that is not funded by either the employee or employer contributions is the supplemental cost.

   Mr. Custis continued his presentation and reviewed the projected benefit funding ratio tables for all the plans. Sen. Morse noted that under statutory provisions, if PERA-P&F continues to exceed the full funding ratio after the 1998 valuations, contribution rates will be reduced to bring them to a funding ratio of ½ percent over full funding. Mr. Custis noted that of the 40 consolidation accounts, only six municipalities had to increase contributions. If not for high investment returns, other municipalities would have had to increase their contributions to the consolidated police and fire funds. Mr. Custis noted that the three first class city funds show a projected deficiency in their funding ratios. Sen. Morse questioned why the 1997 valuations showed MTRFA and StPTRFA with slight sufficiencies but in this table they show deficiencies. Mr. Custis stated that this table projects forward future contributions and discounts them back based on the future payroll. Two things occurred that caused this. The large one-time state contribution and the statutory future direct state aid is defined in a level dollar amount and when considered in conjunction with contributions as a percentage of pay, assuming a growing payroll, that causes the level dollar amount to become a shrinking percentage of pay in the future. He also noted that there is a shift between basic and coordinated members and since basic members have higher employer and employee contributions and the shift is weighted toward an increasing number of coordinated members, the projection assumes lower contributions.

Sen. Morse questioned the impact changing the asset valuation method would have on these funds. Mr. Custis referred members to the last table in their booklets. He stated that the proposed asset valuation method would have produced significantly higher asset recognition for the first class city teacher plans but for the other plans, with the exception of MERF, the proposed asset valuation method would have produced significantly lower asset recognition. He explained that the current asset valuation method fluctuates considerably based on manager style, whether the manager frequently buys and sells or the fund changes managers frequently compared to a manager who buys and holds. The proposed asset valuation method is designed to smooth fluctuations, is based on market value and has no relationship to cost, and eliminates managers style or decisions with regard to the manager. Discussion followed.

Mr. Custis reverted to the table on the funding status of the consolidated police and fire funds. His major point on this table was that the funds indicated have a potential to have a funding shortage over the next five years if all the individuals who may be eligible to retire actually retire.

Sen. Morse took note that at 2:55 P.M. there was a quorum present.

Sen. Morse asked Mr. Custis what the consequences would be if the Commissions didn't change the method of valuing assets. Mr. Custis stated one effect is that DTRFA had a 16% to 17% return on their total assets but in the 1997 valuations a lot of that return was not recognized and what was recognized was paid to the retirees in a post retirement benefit adjustment so DTRFA actually posted an asset loss. Another effect is that some investment decisions have a significant impact on the asset value. Sen. Morse stated that by approving the proposed method of valuing assets it would more directly sever the connection between investment decisions and what happens in valuations so investors can do what is best for investment purposes without manipulating the short term assessment of the fund.

Sen. Morse referred members to the colored chart on the funding and allocation of state aids and noted that he will make sure this item is available to members whenever the state aid issue comes before the Commission.

8. S.F. xxx (Morse); H.F. xxx ( ): Judges Retirement Plan; Increasing Salary and Contributions

Sen. Morse stated that he is having a bill jacketed that deals with this issue and there is a draft included in members' packets. He stated that this proposal addresses the inequities in the funding of the judges plan by moving the judges contributions up to approximately half of normal cost. The proposal increases judicial salaries by 1.5 percent, increases the judges contribution from 6.27 to 8 percent of salary, and lowers the employer contribution by 1.5 percent of salary.

Sen. Betzold asked whether there was any diminishment of judges salaries that might raise the Constitutional issue. Sen. Morse stated that there is a one quarter percent out of pocket expense for the judges but he believes that the judges support this proposal and it is not expected to cause any legal problems. Rep. Kahn asked if the proposal contained language to prevent the judges from getting the salary increase if they did not agree to the increased contribution? Sen. Morse agreed to add that provision.

Edward Burek, LCPR Deputy Executive Director, referred members to the table on page 3 of the staff memo. He noted that the judges do have the lowest percentage of normal cost contribution rate of all the plans indicated. Mr. Burek referred members to the first full paragraph on page 3, the second line, and noted that the 60 percent figure is a typo and should be 50 percent. He briefly reviewed the policy issues on this topic.

John Stanoch, President of the Minnesota District Judges Association and District Court judge with Hennepin County, reviewed the background on this issue. He noted that the judges had agreed to meet after the Second Special Session and discuss this issue. They met in December, 1997 and the result of those meetings was that the judges do not want their contribution rate increased but they will not oppose the bill. He stated that this proposal passed the District Judges Association with only one audible dissenting vote.

Rep. Kahn suggested that the condition for receiving the salary increase should be to accept the contribution increase. Judge Stanoch stated that a similar measure was discussed during the Legislative Session and he would be available to work out language that would be acceptable to everyone concerned. Discussion followed and Senator Morse laid this item over to the next meeting to provide an opportunity to draft appropriate language.

2. **Completion of Mandated Study: Retirement Plan Coverage For Legislators and Constitutional Officers (Fifth Consideration)**

Lawrence A. Martin, LCPR Executive Director, reviewed the staff memo on this topic. He noted that the Commission Chair had directed staff to provide further information on shifting past contributions by current legislators and constitutional officers to the MSRS-Unclassified plan. Current members of the Unclassified Plan have the option to shift prior employee and employer contributions plus interest from past public pension plans into the Unclassified Plan. He stated that the legislators and constitutional officers plans do not have a pool of assets to transfer to the Unclassified Plan since their member contributions go into the State's General Fund and there are no concurrent employer contributions. Mr. Martin identified 28 legislators and 1 constitutional officer who are under age 40 and have less than 10 years of service who may potentially be interested in moving to the Unclassified Plan. He stated that if the employee and employer contributions plus interest for that group were transferred, the cost would be about $700,000. Rep. Kahn suggested that the Commission allow a window for current legislators and constitutional officers to make the election to go into the Unclassified Plan and then appropriate the required dollar transfer at that time. Mr. Martin noted that it is not clear whether legislators are entitled to take a refund from the Legislators Retirement Plan currently. He does not know whether this could be construed as being additional compensation and, if so, then it may be necessary to make this change effective after the next general election. Discussion followed.

Mr. Martin reviewed two options for funding the Legislators Retirement Plan and Elective State Officers Retirement Plan. The first option would create a fund for both plans with an initial transfer from the General Fund equal to prior employee contributions plus interest and a matching employer contribution plus interest. It also would require a future contribution equal to the actuarial accrued liability of the plan. The one-time funding to cover past contributions for the Legislators Retirement Plan would be $13.9 million and for the Elective State Officers Retirement Plan it would be $1.3 million. The ongoing annual funding would be $3.3 million for legislators and $75,000 for constitutional officers to amortize the unfunded actuarial accrued liability by 2020. Discussion followed.

Mr. Martin reviewed the second option and stated that this option would create a fund for both plans with a transfer of $41 million from the General Fund that would fully fund the actuarial accrued liability. This option would cost $1.6 million annually. He stated that if the intention was to fund these two plans up to PERA's funding ratio, the cost would be $28.5 million for legislators and $2.7 million for constitutional officers with ongoing funding of $2.3 million annually for legislators and $85,000 for constitutional officers. Rep. Kahn spoke in opposition to funding these plans from the General Fund. Sen. Pogemiller stated that funding these plans is a fiscally responsible action. Sen. Morse noted that the Department of Finance believes the concept of funding these plans has merit. Rep. Kahn recommended permitting legislators and constitutional officers to elect to transfer to the Unclassified Plan and transfer their prior contributions after January 1, 1999. Mark Shepard, House Research Analyst, testified that transferring past employer contributions prior to January 1, 1999, would be unconstitutional but transferring after January 1, 1999, would be constitutional. Rep. Kahn moved her recommendation as stated above. **MOTION PREVAILED**.

Sen. Pogemiller moved that the Commission recommend Option 1 and Option 3 using the PERA funding ratio as the target appropriation so the options would move forward to the respective government operations committees and indicate that the Pension Commission believes the options make good pension sense. This would allow the legislative leadership to determine whether it makes good political and fiscal sense. **MOTION DID NOT PREVAIL.**

3. **Completion of Mandated Study: Local Police and Fire Consolidation Account Fold-in (Fourth Consideration)**

Edward Burek provided background on this issue and the three staff memos on this topic in members packets. Mr. Burek referred members to the January 21, 1998, memo and stated that the law requires the PERA-P&F employee and employer contribution to be reduced when there is a sufficiency in funding greater than .5% of payroll. Since PERA-P&F has had a sufficiency every year since 1967 and the 1997 valuation indicates 3.79% sufficiency, that reduction in contributions will occur on June 30, 1998. Mr. Burek reviewed the three options for folding the local police and fire consolidation accounts into PERA-P&F and the advantages and disadvantages of each of the options. He reviewed three additional factors for Commission consideration. The first factor was that folding-in consolidation accounts with less than full funding could be considered a subsidization of under funded accounts at the expense of fully funded accounts which was raised by the City of Bloomington. Bloomington believes that it should receive a credit toward future contributions. Mr. Burek noted, however, that the State also provided significant pension aids to municipalities for police and fire pension funds. Mr. Burek stated that existing law states that after the last benefit is paid, which will be decades from now, the excess assets are to be returned to the city and used for police or fire purposes, as applicable. Sen. Morse stated that although those funds are there, they are not and will not be accessible for years. The second factor was how to handle relief associations that consolidate after the merger of some or all of the current consolidation accounts. The third factor was the impact on the excess police state aid program of merging local consolidation accounts into PERA-P&F since the excess police state aid is used to fund other aid programs.

Sen. Morse stated that the study mandate was to provide the advantages and disadvantages of folding-in the consolidation accounts. The mandate did not require determining strategies to accomplish folding-in the accounts. He further noted that he had met with a number of the affected parties in informal discussions on this issue. Sen. Morse stated that he had thought that the readjustment of PERA-P&F's contribution rates was going to occur at the end of the next fiscal year but in the review of the staff memo on this topic, he learned that it would occur at the end of this fiscal year and will have an impact on the way the money flows into the other aid programs.

Sen. Pogemiller moved that the Commission accept the staff memo dated 1/21/98 as the Commission report on this issue, put it in report form, and send it to all parties mandated to receive it. **MOTION PREVAILED.**

7. **S.F. 2150 (Lesewski); H.F. 2727 (Mulder): PERA; Retirement Coverage After Hospital Privatization**

Sen. Morse noted that this issue is similar to the hospital mergers the Commission has dealt with in the past. Mr. Burek began to review the issue and noted that this bill mirrors exactly the bills the Commission passed last year. He also reviewed the University of Minnesota Fairview Hospital solution and noted that those employees were provided with special deferred annuity rights in MSRS. Mr. Burek then reviewed the policy issues and potential amendments the Commission may want to adopt to clarify this legislation.

Tom Evenson, Sioux Valley Hospital and Health System, testified in support of this bill and testified that they had done this last year with the Jackson and Tracy hospitals. He also testified in support of amendment LCPR98-19, which provided that the new pension plan should be based on the PERA provisions in effect on the date of the transfer or sale of the medical facility.

Sen. Betzold moved amendment LCPR98-19. **MOTION PREVAILED.**

Sen. Morse asked if the cities involved in the legislation last year had completed the transfer of an amount equal to the employees contribution to the new plan and what was the new plan. Mr. Evenson testified that he did not believe the cities had transferred any funds for employees in the 0-3 year range. He testified that Sioux Valley in conjunction with PERA had analyzed each employee's status with regard to the Rule of 90, and Sioux Valley wrote an agreement with those employees to assure that they were not disadvantaged by the merger and to provide them with an annuity from Sioux Valley Hospitals that would make them whole. Discussion followed.

David Bergstrom, MSRS Executive Director, testified that Fairview Hospital employees continued to receive MSRS service credit only for eligibility for the "Rule of 90" but the extra service credit was not included in calculating their pension benefit when they retired. Discussion followed.

Mary Vanek, PERA Executive Director, testified that the Sioux Valley Health System is providing a nicer supplement than the Fairview Hospital situation. PERA has been providing an analysis of the employee's benefit status up to the date of sale and what that benefit would have been had the employee continued with PERA. Sioux Valley is then picking up that benefit. Mr. Evenson testified that the benefit package for Jackson/Tracy cost more than the benefit would have cost if the hospital had not privatized.

Sen. Pogemiller moved to recommend S.F. 2150 as amended. **MOTION PREVAILED.**

6. **S.F. 986 (Kelley, S.P.); H.F. 1099 (Folliard): PERA-P&F; Permit Annuity Option Change By Certain Retiree**

Mr. Martin reviewed the background on this issue. He noted that the bill was drafted last session and the retiree is now deceased so amendment LCPR97-14 updates the bill. He briefly reviewed the staff memo regarding the optional annuity forms available to public pension members. He stated that this employee selected a single life annuity, subsequently became ill and died and the spouse is not entitled to a benefit. This bill would provide a survivor benefit. He then reviewed the policy issues raised by this bill. The bill is in opposition to the LCPR Principles of Pension Policy which do not permit reopening optional annuity elections. He noted that there is an actuarial liability to provide this survivor benefit and that this bill would set a precedent for the future. Discussion followed.

Sen. Kelley introduced Constance Anderson, the widow of Laun Anderson, a retired Hopkins police officer. He testified that Mr. Anderson did receive an extra $400 per month because he selected a single life annuity. Sen. Kelley referenced two amendments, one the conforming amendment Mr. Martin had referenced, the other amendment related to the mortality gain of $69,000 received by PERA because of Mr. Anderson's early death. The second amendment would convert that mortality gain to an annuity for Ms. Anderson which would be calculated by PERA's actuary and which is currently estimated at $357 a month rather than the $1700 called for in the original bill.

Ms. Anderson testified that in 1996 they went to the PERA office to sign papers and they were told that they could change the single life annuity option by just having special legislation introduced. She testified that they married in 1988, he retired in 1989, and he died in 1997. Ms. Anderson is also a PERA member. Discussion followed.

Sen. Betzold moved amendments LCPR98-14 and LCPR98-18. **MOTION PREVAILED.**

Sen. Morse **LAID OVER** S.F. 986 as amended.

4. **Completion of Mandated Study: Consolidation Options for First Class City Teacher Retirement Funds (Second Consideration)**

Mr. Burek referred members to the memo dated January 20, 1998, which focused on consolidation and merger options for the first class city teacher plans. He reviewed options A to C, which dealt with phasing out the first class city teacher plans, and the advantages and disadvantages of each. Mr. Burek next reviewed options D to F, which were partial consolidation options. Finally, he reviewed options G to I, which were total consolidation options, and the advantages and disadvantages of each.

Sen. Morse stated that the Commission's responsibility is to file a report. Rep. Kahn recommended accepting this memo in report form. Sen. Morse stated that the report should also include written comments from interested parties.

Gordon Grant, an active St. Paul teacher for 40 years, retired for 7 years, and representing the St. Paul Teachers for Retirement Fairness, testified in support of the StPTRFA consolidation with TRA. He testified that the Uniformity Bill passed last Session addressed a number of their concerns but also left discrepancies. Basic members of the StPTRFA still retire with a 2.0 formula compared to Basic teachers at MTRFA (2.5) and TRA (2.2 and 2.7). StPTRFA Coordinated teachers are paying a ½% higher contribution rate for the same benefits. He further noted that portability is an issue and it would not be if the plans consolidated with TRA. He testified that currently the Minneapolis school district is looking for 500 teachers and if the plans were consolidated and portability was no longer an issue, it might be easier for Minneapolis to find those teachers. Mr. Grant referred to an editorial in Thursday's Pioneer Press regarding consolidation and stated that consolidation might lessen the tax burden.

Gene Waschbusch, StPTRFA Secretary-Treasurer, testified that although some StPTRFA benefits are less than TRA's, some benefits are better than TRA's. He noted that StPTRFA has an automatic survivor benefit and they have a better disability benefit for Basic members than TRA. He stated that StPTRFA's contribution is higher than TRA's but last year TRA's contribution was higher. He stated that the information in the staff memo was accurate but consolidation does have a cost.

Karen Kilberg, MTRFA Executive Director, testified that MTRFA will provide a written statement to the Commission so that it can be included in the report. She noted that there are cost implications to consolidating and MTRFA has not looked at those.

Sen. Pogemiller stated that in the short term, the Commission's concerns are the cost of consolidating, benefit protection, and equities across employees. One policy issue to review is whether there is a consumer benefit to a locally administered plan.

Rep. Murphy suggested that anyone providing written comments should provide them to staff and members in advance of the next Commission meeting.

Sen. Betzold recommended changing the LCPR Rules at the next meeting since there are now twelve Commission members.

Sen. Pogemiller noted that the Commission had requested a study by SBI on the recommendations to the Legislature on the most desirable method for evaluating insurance companies for the purposes of 403(b) plans and asked if the Commission was going to review that report. Sen. Morse stated that the report was due February 1, 1998, and was just received so it will be on a future agenda.

The meeting adjourned at 6:10 P.M.

Jean A. Liebgott

Jean Liebgott, Secretary