

Table of Contents

Legislative Commission on Pensions and Retirement	1-8
• Function, and Creation	1
• Composition	2
• Operation and Resources	3
• Level of Proposed Public Pension Legislation	4
• Principles of Pension Policy	5-8
Minnesota Public Pension Plans	9-18
• Growth and Development	9
• Defined Benefit Plans and Defined Contribution Plans	11
• Establishment	12
• Local Police and Salaried Fire Relief Association Consolidations	16
• Major and Statewide Funds and Administrative Entities	18
Plan Demographics	19-25
Actuarial and Related Information	26-57
• Actuarial Reporting on Minnesota Public Pension Plans	26
• Nature of Actuarial Funding	27
• Pattern of Recognizing Pension Costs Over Time	28
• 2006 Minnesota Public Pension Plan Actuarial Valuation Results	29-35
• Minnesota Public Pension Plans Funding Progress of 1957-2006	36
• Charts	37-53
- Funding Ratio Over Time	37-40
- Normal Cost as a Percentage of Payroll	41-42
- Employee and Employer Contribution Rates Over Time	43-44
- Total Requirements vs. Total Support	45-46
- Total Requirements and Total Contributions Over Time	47-49
- Contribution Deficiency/Surplus Over Time	50-51
- Administrative Expenses Over Time	52-53
• Actuarial Gains and Losses (1986-2003)	54-56
• Post-Retirement Increases	57
State Funding Programs (State Aid) for Minnesota Public Pension Plans	58-60
Total Portfolio Time-Weighted Rates of Investment Return	61
Problem/Issue Areas Related to Minnesota Public Pension Plans	62-77
A. Deficit in the Minnesota Post Retirement Investment Fund (MPRIF)	62
B. Appropriate Approach to Providing Public Sector Pension Benefits	65
C. Inadequate Defined Benefit Plan Contribution Rates	66
D. Disparity in Defined Benefit Plan Accrual Rates and Normal Retirement Ages	68
E. Future of Minnesota Local Retirement Plans	69
F. Actuarial Value of Assets	69
G. Unfunded Actuarial Accrued Liability Level Percentage of Pay Amortization	71
H. Appropriateness of Current Actuarial Assumption, Especially Economic Assumptions	72
I. Extent of Active versus Passive Investment Strategies	73
J. State Aid Programs Dedicated to Pension Funding	76
K. Appropriate Manner for the State to Obtain Actuarial Information	77
Glossary of Minnesota Public Pension Terminology	79-83

Minnesota Legislative Commission on Pensions and Retirement

Function and Creation

■ Function of the Pension Commission

- The Pension Commission is a joint agency of the Minnesota Legislature.
- The Pension Commission performs four major functions:
 - i) reviews and makes recommendations to standing legislative committees on pending proposed public pension legislation;
 - ii) conducts ongoing research on pension policy issues;
 - iii) provides legislative oversight for Minnesota's system of over 700 public employee pension plans; and
 - iv) assesses the sufficiency of current public pension plan funding and recommends required modifications.
- The Minnesota Pension Commission is one of almost two dozen state pension commissions nationwide.

■ Creation of the Pension Commission

- Initially established as an Interim Commission
 - 1943 (Laws 1943, Chapter 449)
 - 1955 (Laws 1955, Chapter 829)
 - 1957 (Extra Session Laws 1957, Chapter 13)
 - 1959 (Extra Session Laws 1959, Chapter 82)
 - 1963 (Laws 1963, Chapter 888, Section 9)
 - 1965 (Laws 1965, Chapter 888, Section 5)
- No Pension Commission was established during the 1961-1963 Biennium
- Pension Commission established as a permanent entity in 1967 (Laws 1967, Chapter 549; coded as Minnesota Statutes, Section 3.85)
- Pension Commission is the oldest extant Minnesota Legislative Commission

Legislative Commission on Pensions and Retirement Composition

■ Composition of the Pension Commission

- The Commission consists of five members of the House of Representatives and five members of the Senate
- The House members of the Commission are appointed by the Speaker of the House
- The Senate members of the Commission are appointed by the Subcommittee on Committees of the Senate Rules Committee
- 105 legislators have served on the Commission 1943-2006, during 259 two-year terms (including mid-term vacancies that were filled)
- Length of service by Commission members 1943-2006:

<u>Total Years of Service</u>	<u>Number of Members</u>	<u>Percent of Total</u>
1 Year	4	3.81%
2 Years	40	38.10%
3 Years	1	0.95%
4 Years	20	19.05%
6 Years	21	20.00%
7 Years	1	0.95%
8 Years	3	2.86%
10 Years	6	5.71%
11 Years	2	1.90%
12 Years	3	2.86%
16 Years	1	0.95%
18 Years	1	0.95%
20 Years	1	0.95%
22 Years	1	0.95%

- Geographical distribution of Commission members, by membership number and by Commission membership term 1943-2006

	<u>Number of Members</u>	<u>Percent of Total Membership</u>	<u>Total Terms</u>	<u>Percent of Total Terms</u>
Duluth	1	1.0%	1	0.4%
St. Paul	15	14.3%	32.5	12.5%
Minneapolis	23	21.9%	63.5	24.5%
Suburban Twin Cities	19	18.1%	49	18.9%
Greater Minnesota	47	44.8%	113	43.6%

Legislative Commission on Pensions and Retirement

Operation and Resources

■ Operation of the Pension Commission

- The Commission Chair sets the general direction of the Commission.
- The Commission Chair has a two-year term.
- The Commission Chair alternates between the House and Senate membership; the Chair and other Commission officers are elected from and by the Commission membership.
- After appointment, the Commission typically meets weekly during the Legislative Session until the initial committee bill hearing deadline.
- During the Interim, the Commission typically meets monthly.
- By longstanding agreement, the House and Senate committees with jurisdiction over pensions refrain from hearing proposed pension legislation until receiving a recommendation from the Commission.
- The Commission recommendation of proposed pension legislation requires a majority vote of the total commission membership of both the House and the Senate; all other Commission actions require simple majority vote of Commission members in attendance.
- The Commission recommendation on proposed pension legislation is typically accompanied by Commission-approved amendments.
- Commission recommended proposed pension legislation is typically consolidated into one or a small number of "Omnibus" Pension Bills.
- Commission recommended proposed pension legislation affecting pension benefits is typically accompanied by an actuarial cost estimate, generally prepared by the actuary retained jointly by the statewide and major local retirement administrations.

■ Staffing of the Commission

- The Commission employs a permanent staff of 3.5 full-time equivalent positions.

■ Actuarial Resources

- The actuarial work for most Minnesota defined benefit plans is prepared by a consulting actuarial firm retained jointly by the seven largest retirement systems.
- The Commission can utilize the services of the jointly retained actuary.

Legislative Commission on Pensions and Retirement Level of Proposed Public Pension Legislation

■ General Level of Public Pension Legislation

- Historically, an average of 78 public pension bills are introduced annually
- Commission typically reviews 85 percent of proposed pension legislation introduced
- Typically, 40 introduced public pension bills annually are ultimately heard in some form by standing committees
- Proposed pension legislation typically covers a broad range of plans and circumstances:

25 percent related to major statewide plans

13 percent related to minor statewide plans

6 percent related to local general employee plans

15 percent related to police and paid fire pension plans

8 percent related to volunteer fire relief associations

20 percent related to individual or small group requests

13 percent related to miscellaneous pension topics

Legislative Commission on Pensions and Retirement

Principles of Pension Policy

I. Preamble

The Legislative Commission on Pensions and Retirement recommends the following statement of principles, which have been developed since 1955, as the basis for evaluating proposed public pension legislation. Problems can be avoided or minimized if a sound set of principles is used as a guideline in developing the various public pension funds and plans.

II. Substantive Principles

A. Purpose of Minnesota Public Pension Plans

1. Minnesota public pension plans exist to augment the Minnesota public employer's personnel and compensation system by assisting in the recruitment of new qualified public employees, the retention of existing qualified public employees, and the systematic outtransitioning of existing public employees at the normally expected conclusion of their working careers by providing, in combination with federal Social Security coverage, personal savings and other relevant financial sources, retirement income that is adequate and affordable.
2. Minnesota public pension plans should play their appropriate role in providing financial security to public employees in retirement.
3. As Minnesota public employee workforce trends develop, Minnesota public pension plans should be sufficiently flexible to make necessary adaptations.

B. Structure of Minnesota Public Pension Coverage

1. Creation of New Pension Plans
 - a. Minnesota public employers, on their own initiative, without legislative authorization, should not be permitted to establish or maintain new public pension plans, except for volunteer firefighter relief associations.
 - b. New pension plans for volunteer firefighters should be organized on a county or comparable regional basis if possible.
2. Mandatory Public Pension Plan Membership

To the extent possible, membership in a public pension plan should be mandatory for the personnel employed on a recurring or regular basis.
3. Consolidation of Public Pension Plans by a Minnesota Public Employer.
 - a. The State, with the second largest number of public employee pension plans in the nation, would benefit from a more rational public pension plan structure.
 - b. The voluntary consolidation of smaller public pension plans should be encouraged, with the development of county or comparable regional public employee pension plans in place of a large number of small local plans to assist in this consolidation if a statewide public pension plan is deemed to be inappropriate.

C. Pension Benefit Coverage

1. General Preference for Defined Benefit Plans Over Defined Contribution Plans
 - a. Defined benefit plans, where they currently exist, should remain as the primary retirement coverage for Minnesota public employees.
 - b. Defined contribution plans are particularly appropriate where interstate portability or private sector-public sector portability is a primary consideration of the public employee group, where the public employee group lacks civil service or analogous employment protections, or where the defined contribution plan is a supplemental pension plan.
2. Social Security Coverage

Except for public employees who are police officers or firefighters, coverage by the federal Old Age, Survivors, Disability and Health Insurance (Social Security) Program should be part of the retirement coverage for Minnesota public employees.
3. Equal Treatment Within Pension Plans

There should be equal pension treatment of public employees in terms of the relationship between benefits and contributions.
4. Appropriate Normal Retirement Ages

The normal retirement age should be set in a reasonable relationship to the employability limits of the average public employee and should differentiate between regular public employees and protective and public safety employees.
5. Appropriate Early Retirement Reductions

Public employee pension plans should not subsidize early retirement benefits and, except for appropriately designed early retirement incentive programs, retirement benefits should be actuarially reduced for retirement before any applicable normal retirement age.
6. Uniformity and Equal Benefit Treatment Among Plans

There should be equal pension treatment in terms of the relationship between benefits and contributions among the various plans and, as nearly as practicable, within the confines of plan demographics, retirement benefits and member contributions should be uniform.
7. Adequacy of Benefits at Retirement
 - a. Benefit adequacy requires that retirement benefits respond to changes in the economy.
 - b. The retirement benefit should be adequate at the time of retirement.
 - c. Except for local police or firefighter relief associations, the retirement benefit should be related to an individual's final average salary, determined on the basis of the highest five successive years average salary unless a different averaging period is designated by the Legislature.

Legislative Commission on Pensions and Retirement

Principles of Pension Policy

- d. Except for local police or firefighter relief associations, the measure of retirement benefit adequacy should be at a minimum of thirty years service, which would be a reasonable public employment career, and at the generally applicable normal retirement age.
 - e. Retirement benefit adequacy must be a function of the Minnesota public pension plan benefit and any Social Security benefit payable on account of Minnesota public employment.
8. Postretirement Benefit Adequacy
 - a. The retirement benefit should be adequate during the period of retirement.
 - b. Postretirement benefit adequacy should function to replace the impact of economic inflation over time in order to maintain a retirement benefit that was adequate at the time of retirement.
 - c. The system of periodic post retirement increases should be funded on an actuarial basis.
 - d. In order to replace inflation, the post retirement adjustment system should follow a valid recognized economic indicator.
 9. Portability

To the extent feasible, portability should be established as broadly as possible for employment mobile public employees.
 10. Purchases of Prior Service Credit

Purchases of public pension plan credit for periods of prior service should be permitted only if, on a case-by-case basis, it is determined that the period to be purchased is public employment or substantially akin to public employment, that the prior service period must have a significant connection to Minnesota, that the purchase payment from the member or from a combination of the member and the employer must equal the actuarial liability to be incurred by the pension plan for the benefit associated with the purchase, appropriately calculated, without the provision of a subsidy from the pension plan, and that the purchase must not violate notions of equity.
 11. Deadline Extensions and Waivers

Deadline extensions or waivers should be permitted only if, on a case-by-case basis, it is determined that there is a sufficient equitable basis for the extension or waiver, the extension or waiver does not involve broader applicability than the pension plan members making the request, and that the extension or waiver is unlikely to constitute an inappropriate precedent for the future.
 12. Vesting Requirement Waivers

Waivers of vesting requirements should be permitted only if, on a case-by-case basis, it is determined that there is a strong equitable argument to grant the waiver for the requesting public employees.
 13. Reopening Optional Annuity Elections

Reopenings of optional annuity elections should not be permitted.
 14. Benefit Increase Retroactivity

Retroactivity of benefit increases for retirees and other benefit recipients should not be permitted.
 15. Repayment of Previously Paid Benefits and Resumptions of Active Member Status

Repayments of previously paid benefits and resumptions of active member status should not be permitted.
 16. Duplicate Public Pension Coverage for the Same Employment

Unless supplemental pension plan coverage is involved, public employees should not have coverage by more than one Minnesota public pension plan for the same period of service with the same public employer.
 17. Reemployed Annuitant Earnings Limitations
 - a. Limitations on the earnings by reemployed annuitants should apply only to the reemployment of an annuitant by an employing unit that is a participating employer in the same public pension plan from which the annuitant is receiving a pension benefit.
 - b. Reemployed annuitant earnings limitations should be standardized to the extent possible among the various Minnesota public pension plans.
 18. Disability Definitions

The definitions of what constitutes a disability giving rise to a disability benefit should be standardized to the extent possible, recognizing the differences in the hazards inherent in various types of employment.
 19. Design of Early Retirement Incentive Programs
 - a. Early retirement incentive programs can have a valid role to play in the public sector personnel system.
 - b. Early retirement incentive programs should be targeted to situations when a public employer needs to reduce staffing levels beyond normal attrition.
 - c. Early retirement incentive programs should be financed appropriately, with the cost of the benefits provided under the early retirement incentive program borne wholly by the same public employer that gains any compensation savings from a staffing level reduction, without any subsidy from the affected public pension plan.
 20. Future Pension Coverage for Privatized Public Employees

Because of applicable federal regulation, employees of public employers that are privatized should not be allowed to continue public pension plan coverage in the future. Privatized public employees should receive adequate replacement pension coverage and a better resolution of this topic should be raised with appropriate federal government officials.

Legislative Commission on Pensions and Retirement

Principles of Pension Policy

21. Supplemental Pension Plans

- a. Public employees should be encouraged to engage in personal savings for their retirement.
- b. The State should assist this process by making personal retirement savings opportunities available to public employees.
- c. Public employers should have an opportunity to elect to provide financial support to established supplemental pension arrangements for their employees.

22. No Intended Ultimate Benefit Diminutions

- a. In recommending benefit plan modifications, the imposition of reductions in overall benefit coverage for existing pension plan members should not be recommended.
- b. The imposition of a reduction in overall benefit coverage may be imposed for new pension plan members in order to achieve sound pension policy goals.
- c. A reduction in some aspect or aspects of benefit coverage may be recommended in combination with a proposed benefit increase or benefit increases in implementing sound pension policy goals.

D. Pension Plan Funding

1. Equal Pension Financing Burden for Generations of Taxpayers

There should be utilized a financing method that will distribute total pension costs fairly among the current and future generations of taxpayers and that will discourage unreasonable benefit demands.

2. Actuarial Funding of Pension Benefits

- a. Retirement benefits in Minnesota defined benefit plans should be funded on an actuarial basis.
- b. Currently earned pension plan service credit, as measured by the actuarially determined entry age normal cost of the defined benefit pension plan, should be funded on a current basis.
- c. The administrative expenses of the defined benefit pension plan should be funded on a current basis.
- d. Existing unfunded actuarial accrued liabilities of the defined benefit pension plan should be amortized over a reasonable period of time, and that amortization period should be related to the average working career of the membership of the pension plan, but not to exceed forty years.

3. Allocation of Funding Burden Between Members and Employers

- a. Retirement benefits should be financed on a shared basis between the public employee and the public employer.
- b. For general public employees, the employee and employer should make matching contributions to meet the normal cost and the administrative expenses of the defined benefit pension plan and both the employee and the employer may be required to share some financial

responsibility for funding the amortization requirement of the defined benefit pension plan.

- c. For protective and public safety employees covered by a statewide public pension plan, the employee should pay forty percent of the total actuarial costs of the defined benefit pension plan and the employer should pay sixty percent of the total actuarial costs of the defined benefit pension plan.
- d. For protective and public safety employees covered by a local relief association, employee and employer contributions should be considered in light of the special circumstances and history unique to that association. Employees should pay an appropriate portion of the normal cost and administrative expenses of the relief association.

4. Funding of Postretirement Adjustments

- a. Ad hoc postretirement adjustments should be funded separately from the regular defined benefit public pension plan financing and should not be added to the unfunded actuarial accrued liability of the defined benefit public pension plan.
- b. Automatic postretirement adjustment mechanisms should be funded on an actuarial basis as part of the actuarial requirements and contribution structure of the defined benefit public pension plan.

5. Appropriate Basis for Actuarial Assumption Changes

- a. Actuarial assumption changes should only be based on the results of the gain and loss analyses in the regular actuarial valuation reports and the results of a periodic experience study.
- b. Actuarial assumption changes should stand on their own merit, and should not be changed solely to improve benefits or to lower contribution rates.

6. Appropriate Basis for Modifying Contribution Rates

Member and employer contribution rates should only be modified based on the trend in total support rate deficiency or sufficiency revealed in the regular actuarial valuation reports.

E. Pension Plan Investments

1. Appropriate Investment of Public Pension Assets

- a. Public pension plan investment authority should be as uniform as is practicable.
- b. Public pension plan investments should be made in accord with the prudent person rule.
- c. Public pension plan investment authority should be further regulated by a list of authorized investment types, which should appropriately differentiate between pension plans based on asset size and investment expertise.
- d. Written investment policies should be maintained for the investment of public pension plan assets.
- e. Public pension plans should regularly report on their investments, including performance.

Legislative Commission on Pensions and Retirement

Principles of Pension Policy

2. Sole Membership Benefit Dedication of Plan Assets

Recognizing that public pension plan assets exist to defray current and future pension benefit payments, public pension plan assets should be dedicated to the sole benefit of the plan membership in their investment and expenditure.

F. **Compliance With Federal Pension Plan Regulation**

Consistent with the principles of federalism, dual sovereignty, and comity among governmental entities, public pension plan provisions and administrative operations and activities should attempt to comply with applicable federal pension plan regulation in order to maintain the tax qualified status of public pension plans.

G. **Public Pension Plan Fiduciary Responsibility**

1. Strong Fiduciary Responsibility Standards

Public pension plan activities should be conducted in accord with strong fiduciary responsibility standards and regulation.

2. Remedies for Fiduciary Breach

Failures to conduct public pension plan activities in accord with the applicable fiduciary responsibility standards and regulation should be subject to appropriate fiduciary breach remedies.

III. **Procedural Principles of Pension Policy**

A. **Adequate Pension Funding**

1. Pre-Existing Funding

No proposed increase in pension benefits for any public pension plan should be recommended by the Legislative Commission on Pension and Retirement until there is established adequate financing to cover the pre-increase normal cost, administrative expense, and amortization contribution requirements of the defined benefit public pension plan calculated according to the applicable actuarial reporting law.

2. Funding Increase

No proposed increase in pension benefits for any defined benefit public pension plan should be recommended by the Legislative Commission on Pensions and Retirement unless there is included, in the proposal, adequate financing to meet any resulting increase in the normal cost and amortization contribution requirements of the defined benefit public pension plan that are estimated by the applicable actuary to result from adopting the proposed benefit increase.

B. **Preference for General Legislation**

No pension legislation of local or special limited application should be recommended by the Legislative Commission on Pensions and Retirement if the purpose and the intent of the proposed legislation would be better served by legislation of general statutory application or if the proposed legislation constitutes a significant departure from previously established

uniform pension policy. Pension legislation affecting local police or salaried firefighters may be recommended by the Legislative Commission on Pensions and Retirement in light of any special circumstances that are unique to the relief association.

C. **Explicit Application of Principles of Pension Policy**

1. Measurement Against Principles

Each proposed change in retirement benefits or financing should be measured by the Legislative Commission on Pension and Retirement against the current principles of pension policy as part of its consideration to insure that there is adherence to sound pension policy.

2. Formal Reporting of Consistency

The Commission's determination concerning compliance with the principles of pension policy should be a part of the Commission's formal report of its recommendations on proposed public pension legislation.

Revised 12/6/96

