

TO: Members of the Legislative Commission on Pensions and Retirement

FROM: Lawrence A. Martin, Executive Director

RE: S.F. 1682 (Pogemiller); H.F. xxx: PERA; Defining Covered Salary to Include Certain Employer Contributions to Supplemental Retirement Plans

DATE: March 29, 2005

Summary of S.F. 1682 (Pogemiller); H.F. xxx

S.F. 1682 (Pogemiller); H.F. xxx amends Minnesota Statutes, Sections 353.01, Subdivision 10, and 356.24, Subdivision 1, the definition of salary for the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General) and the specification of exceptions from a general ban on employer-funded supplemental retirement plans, by making the following changes:

1. Includes Various Supplemental Plan Employer Contributions in PERA-General Covered Salary. The amount of contributions to the laborers national industrial pension fund, the plumbers and pipefitters national or local pension fund, and to the International Union of Operating Engineers pension fund made by local government employers under Minnesota Statutes, Section 356.24, as supplemental retirement plans would be included in covered salary by PERA for contribution and retirement benefit purposes and permits equivalent member and employer contributions on those amounts during the period 2002-2005 (Sections 1 and 3);
2. Extends Supplemental Retirement Plan Status to Laborers Local Pension Fund. In addition to the laborer's national industrial pension fund, coverage by a laborers local pension fund is exempt from a general restriction on employer-funded supplemental pension plans (Section 2); and
3. Increases Trade Union Pension Fund Supplemental Pension Plan Employer Contribution Maximum to \$5,000. The current \$2,000 annual maximum on employer contributions to trade union pension funds as permissible supplemental pension plan contributions is increased to \$5,000 (Section 2).

Supplemental Plan Coverage Issues for IUOE Local 49 and Laborers Union

In a letter from Mike Wilde, General Counsel, International Union of Operating Engineers, Local 49, and attachments to that letter relating to Local 49 and the Laborers Union, there are three issues:

1. PERA-General Definition of Salary Excludes Supplemental Plan Contribution. International Union of Operating Engineers Local 49 members are authorized under Minnesota Statutes, Section 356.24, Subdivision 1, Clause (10), to retain their union pension coverage as supplemental coverage in addition to retirement coverage by the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General), but PERA has determined that those employer supplemental retirement plan contributions are not includable in the definition of covered salary for PERA-General contributions and benefits. Local 49 believes that these contributions should be included in the PERA-General covered salary figure.
2. Add Minnesota Laborers Pension Fund as Authorized Supplemental Retirement Plan. The Laborer's National Industrial Pension Fund is currently an authorized supplemental retirement plan and the Laborer's Union seeks to add the Minnesota Laborer's Pension Fund as an alternative supplemental retirement plan.
3. Maximum Supplemental Retirement Plan Contribution Increase. The supplemental retirement plan contribution to the Laborer's National Industrial Pension Fund, to the Plumbers and Pipefitters National Pension Fund or a local plumbers and pipefitters pension fund, and to the International Union of Operating Engineers Pension Fund has a current maximum of \$2,000 and those organizations are seeking an increase in the maximum to \$5,000.

Background Information on the Definition of Covered Salary for Minnesota Defined Benefit Plans

Background information on the definition by the Minnesota general employee defined benefit plans of covered salary for retirement plan contributions and benefits is set forth in Appendix A.

Background Information on Public Retirement Plan Coverage for Government Trades Personnel

For most trades personnel, pension coverage for their employment is typically provided through a Taft-Hartley Act jointly (union and employer(s)) trustee union pension plan. These union pension plans typically have break-in-service rules whereby prior service credit in the plan can be forfeited by virtue of an extended interval without plan contributions and coverage. As a result, trades personnel employed in the public sector who have had prior private sector trade employment or who are contemplating future private sector trade employment after their public sector trade employment ends frequently retain union pension plan coverage in addition to the public pension plan coverage while in public sector trade employment. Since public employers generally are unwilling to pay more than private sector trade wage scale and benefit costs, the cost of the public pension plan employer contribution is deducted when setting the trade person's hourly rate. In this way, many trades personnel end up with double pension coverage for their public employment, for which they typically bear the full member and employer contribution cost for the public pension plan coverage. The double pension coverage, at the full member and employer contribution cost to the tradesperson, may be undesired coverage from the perspective of the tradesperson and may be excessive coverage from a pension policy perspective. Some trades personnel have attempted to reduce their ongoing pension contribution load by seeking exclusions from the public pension plan coverage. These exclusions have been approved by the Legislature on three prior occasions, for the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General) with respect to various trades personnel at the Metropolitan Council Environmental Services waste treatment plant (the former Metropolitan Waste Control Commission facility) (see Laws 1977, Chapter 98), for PERA-General with respect to pipefitters and associated trades employed by the St. Paul School District (see Laws 1997, Chapter 241, Article 2, Sections 1, 8, and 12), and for PERA-General with respect to electrical workers, plumbers, carpenters, and related trades personnel employed by either the City of St. Paul or the St. Paul School District (see Laws 2000, Chapter 461, Article 7, Sections 1, 4, and 5), and for PERA-General with respect to bricklayers, allied craftworkers, cement masons, glaziers, glassworkers, painters, allied tradesworkers, and plasterers employed by the City of St. Paul or Independent School District No. 625, and with respect to plumbers employed by the Metropolitan Airports Commission (see First Special Session Laws 2001, Chapter 10, Article 10, Section 2).

While some trades personnel have sought an exclusion from public pension plan coverage, chiefly the City of St. Paul, the St. Paul Public Schools, and the Metropolitan Airports Commission, some other trades personnel in the public sector have sought authority for the union pension plan to function providing additional coverage as supplemental retirement plans under Minnesota Statutes, Section 356.24.

The trade union pension funds involved are the Laborer's National Industrial Pension Fund (2001), the Plumbers and Pipefitters National Pension Fund (2002), and the International Union of Operating Engineers Pension Fund (2002).

Background Information on Supplemental and Local Pension Plan Restrictions.

Minnesota Statutes, Section 356.24, when initially enacted in 1971 (Laws 1971, Chapter 222, Section 1), was intended to end a growing 1960s practice in local government (primarily by school districts) of creating supplemental employer-funded pension plans beyond the regularly applicable statewide pension plan for that type of public employee. At that time, public pension benefits were considerably more modest than they are currently and some of the more affluent jurisdictions were attempting to readjust their employees' pension coverage by local action, without the approval of or notice to the Legislature. The Legislature decided that this practice was inappropriate and that the creation of additional pension plans was an unwise policy. The Legislature also apparently felt that pension benefits should be as uniform as possible geographically throughout public employment. In 1973, the Legislature considerably improved pension benefits payable under the public employees primary pension coverage by moving from career average salary plans to pensions that were based on the average salary of the individual close to retirement. The intent at the time was to provide an adequate retirement benefit through the primary pension plan and eliminate the need, or the ability, to create supplemental plans. Those supplemental plans that were in effect prior to 1971 were grandfathered. Substantial statewide general employee retirement plan benefit increases occurred in 1980, 1989, 1992, and 1997.

A number of exceptions to the restriction on supplemental employer-funded pension plans have been enacted. Beyond the pre-1971 grandfathered supplemental pension plans, the 1971 legislation also excluded from its application group health, hospital, disability, or death benefits. In 1980 (Laws 1980, Chapter 600, Section 7), an exception was added for severance pay plans authorized under Minnesota Statutes, Section 465.72. In 1988 (Laws 1988, Chapter 605, Section 9), the State Deferred Compensation Program was modified to include a matching employer contribution in addition to the member's deferred compensation amount. The State Deferred Compensation Program is governed by Minnesota Statutes, Section 352.96. The State Deferred Compensation Program is the sole government sponsored retirement

thrift or savings program for most public employees. Although the plan is administered by the Minnesota State Retirement System (MSRS), public employees throughout the state are authorized to participate. For purposes of the State Deferred Compensation Program, public employment includes volunteer firefighters. The State Deferred Compensation Program, akin to the somewhat similar Internal Revenue Code, Section 403(b), plans, function to encourage additional saving for retirement, supplementing income during retirement from the primary public pension plan, Social Security, or other income sources. State Deferred Compensation Program was established in 1971, by Extra Session Laws 1971, Chapter 32, Section 19. The matching employer contribution to the State Deferred Compensation Plan, authorized under Minnesota Statutes, Section 356.24, under the 1988 legislation was required to be made solely to the State Deferred Compensation Program, was required to be provided for in either a personnel plan or a collective bargaining agreement, was required to be a dollar for dollar match, and was limited to \$2,000 per year per employee. While not restricted in use to fund retiree health insurance premiums, the employer matching contribution authorization was part of a broader legislative enactment pertaining to retiree health benefits, and the conferees on Laws 1988, Chapter 605, discussed the potential for the savings promoted by the employer matching contribution authorization to be used in part to defray post-retirement health insurance premium costs.

In 1992 (Laws 1992, Chapter 487, Section 4), similar authority for an employer matching contribution feature for teacher tax-sheltered annuity insurance contracts under federal Internal Revenue Code, Section 403(b), was established by adding an additional exception to Minnesota Statutes, Section 356.24. The applicable tax-sheltered annuity insurance contracts are those issued by one of up to ten qualified insurance companies licensed to do business in this state, engaged in the life insurance or annuity business, determined by the Commerce Commissioner to be among the top two rating categories of a national insurance rating entity, and selected by the Minnesota State Board of Investment as providing competitive options and investment returns. Internal Revenue Code, Section 403(b), tax-sheltered annuity plans are vehicles for teachers, church workers, and certain other personnel of charitable institutions, to save on a tax deferred basis. These plans are not any public employee's primary retirement coverage; rather they act to supplement the primary plan. This permits eligible employees to have some individual control over their eventual retirement income. Internal Revenue Code, Section 403(b), investments are generally referred to as tax-sheltered annuities.

Also, in 1988 (Laws 1988, Chapter 709, Article 11), with the creation of the State University System/Community College System Individual Retirement Account Plan (IRAP), an exception for the IRAP Plan was added to Minnesota Statutes, Section 356.24. In 1989 (Laws 1989, Chapter 319, Article 12, Section 3), employer contributions to the Higher Education Supplemental Retirement Plan, established in 1965, were exempted from the application of the supplemental pension plan restriction of Minnesota Statutes, Section 356.24.

In 2001, two additional exceptions were added to the supplemental retirement plan restriction of Minnesota Statutes, Section 356.24. The exceptions are for employer contributions to a supplemental plan or governmental trust established for post-retirement health care expenses under the federal Internal Revenue Code as set in the employer's personnel policy or set by a collective bargaining agreement and for employer contributions up to \$2,000 annually to the Laborer's National Industrial Pension Fund as set in a collective bargaining agreement. In 2002 (Laws 2002, Chapter 392, Article 10, Section 1), additional exceptions for the Plumbers and Pipefitters National Pension Fund and for the International Union of Operating Engineers Pension Fund were added to the supplemental retirement plan restriction of Minnesota Statutes, Section 356.24, with a \$2,000 annual maximum on the employer contributions to each of the two new supplemental retirement plans. In 2003 (First Special Session Laws 2003, Chapter 7, Section 1), the exceptions for the Plumbers and Pipefitters National Pension Fund was broadened to include alternatively a plumbers and pipefitters local pension fund.

Discussion and Analysis

S.F. 1682 (Pogemiller); H.F. xxx would redefine the term "salary" in the law governing the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General) to include the amount of employer contributions to a trade union pension fund operating as a permitted supplemental retirement plan under Minnesota Statutes, Section 356.24, with a "catch-up" equivalent contribution authority to cover the period 2002-2005, would authorize a laborer's local pension fund as a permitted supplemental retirement plan, and would increase the maximum employer contribution to a trade union supplemental pension plan from \$2,000 annually to \$5,000 annually.

The proposed legislation raises several pension and related public policy issues that may merit Commission consideration and discussion, as follows:

1. Inconsistent Policy on Providing Pension Coverage for Trade Union Personnel Employed by Local Government Units. The policy issue is the appropriateness of this additional complication in the current inconsistent policy of providing pension coverage for trade union and related personnel who are employed by local governmental units in Minnesota. Trades personnel in Minnesota public employment have three alternative ways in which they have pension coverage, either coverage solely by a general public employee retirement plan (either by the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General) or by the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General)), coverage solely by their trade union pension plan (most or all trade union personnel employed by the City of St. Paul, ISD No. 625, the Metropolitan Council Environmental Services Division, and the Metropolitan Airports Commission), or coverage by both a general public employee retirement plan and a trade union pension plan (laborers, plumbers, pipefitters, and operating engineers). Trade union personnel with general public employee retirement plan coverage only risk portability problems and benefit losses if the employee is employed in the public sector only for a short period of time in the middle of the person's career, because of the break-in-service rules typically used by labor union pension plans. Trade union personnel with union pension plan coverage only have benefit coverage identical to their trade union counterparts in the private sector, but a tradesperson with long public service might or might not have pension coverage identical or comparable to other public employees. Trades personnel with full general public employee retirement plan coverage as primary retirement plan coverage and with trade union pension fund coverage as supplemental retirement plan coverage will have greater coverage than either the typical public employee or the typical tradesperson. If some or all of the changes in the proposed legislation are enacted, this disparity in benefit coverage will be further complicated. The Commission should consider taking additional testimony about and engaging in additional consideration of the appropriate manner for providing retirement coverage for trades personnel in the public sector, either in a future hearing during this Session or as a future Commission interim project.
2. Unclear Policy on the Role of Supplemental Retirement Plans for Public Sector Employees. The policy issue is the appropriateness of making more complex the role and function of supplemental retirement plan coverage for public sector employees. In order to prevent the growth of very disparate and highly variable public sector retirement benefits in 1971, the Legislature enacted a blanket restriction on the creation of new supplemental retirement plans. In 1988, the Legislature shifted from a general ban on supplemental retirement plans to actual encouragement of the creation of thrift or savings plans as supplemental retirement plans, with a \$2,000 annual maximum on the employer contribution to these types of defined contribution plans. The \$2,000 annual employer contribution maximum has been retained, with the sole exception of a bargained maximum for the Minnesota State Colleges and Universities System (MnSCU) Higher Education Supplemental Retirement Plan. Since 2001, with the authorization of trade union pension plans as supplemental pension plans, defined benefit retirement plans were added as supplemental retirement plans, and now the proposal is to increase the number of trade union pension plans as much and to increase the maximum employer contribution permitted for these plans. While the Commission staff has limited information on the extent of the utilization of these thrift/savings plan supplemental retirement plans, it is clear that the development of these supplemental retirement plans has been varied and inconsistent and that their benefit output is far from uniform or consistent. The wisdom of making this situation more complex and diverse as proposed is unclear and would merit additional consideration either during the legislative session or during the interim.
3. Appropriateness of Redefining "Salary" for PERA-General to Include Employer Supplemental Retirement Plans. The policy issue is the appropriateness of defining "salary" for the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General) to include some employer contributions to supplemental retirement plans. The definition of "salary" drives the final average salary amount on which retirement benefits are calculated as well as driving member and employer contribution amounts. The purpose of the definition of "salary" is to establish a reliable estimate of the standard of living level on which retirement benefits may be based. The "salary" definition is not to include one-time payments, such as severance pay, or other compensation items that are not recurring or that are not reflective of a plan member's standard of living. It is unclear whether or not the employer-paid contributions to trade union pension plans as supplemental retirement plans is actually a portion of an employee's standard of living, since these are potentially not voluntary. The International Union of Operating Engineers, Local 49, legal counsel argues that these employer supplemental retirement plan contributions are identical to member contribution deductions for supplemental retirement plans. Because public employers likely reduce the actual hourly compensation rate of trades personnel by the amount of these employer supplemental retirement plan contributions, so that the public sector package cost is identical to the private sector

package cost, International Union of Operating Engineers Local 49 General Counsel Mike Wilde's contention of comparability has a factual basis. PERA, which has determined that these amounts are not identical to member supplemental retirement plan contribution deductions, may be able to shed more light in testimony on the appropriateness issue.

4. Appropriateness of the Optional "Back" Contribution Authority. The policy issue is whether or not it is appropriate to permit trades personnel with past employer contributions to trade union pension funds to gain past additional salary credit from the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General). The loss of past PERA-General salary credit will be of importance to any trades personnel who are in their final five years of public employment, so they are the individuals most likely to want to gain this credit by the payment of back contribution amounts, especially if the addition to the highest five successive years average salary figure produces a higher PERA-General benefit. Because the back contribution option is likely to be used only by those tradespersons who will be the most likely to benefit, this is an "election against the pension fund" opportunity that will likely produce a larger PERA-General accrued liability than the contributions to be received, as the Commission discovered with similar prior service credit purchases. That "election against the pension fund" imposition of additional unfunded actuarial accrued liability could be avoided if all trades personnel were required, rather than permitted, to make the "back" equivalent contributions.
5. Appropriateness of Including Local Union Pension Fund in Addition to National Union Pension Fund as Supplemental Retirement Plan. The policy issue is the appropriateness of adding a local trade union pension plan as an authorized supplemental retirement plan in addition to the national trade union pension plan. The proposal is the inclusion of the laborer's local pension fund. The Laborer's National Industrial Pension Fund was the first trade union pension plan to be added as a supplemental retirement plan. The authorization of the local plumbers and pipefitters local pension fund as a supplemental retirement plan was added to the Plumbers and Pipefitters National Pension Fund and is the precedent for the change. It is unclear why the laborer's union did not pursue both the national union pension fund and the local union pension fund back in 2001 when it first gained the authorization of a trade union pension fund as a supplemental retirement plan. Some additional testimony from the laborer's union should be requested to explain the shift at this time.
6. Appropriateness of Increasing the \$2,000 Trade Union Employer Supplemental Retirement Plan Contribution Maximum. The policy issue is the appropriateness of increasing the \$2,000 annual employer supplemental retirement plan contribution maximum to \$5,000 for the three trade union supplemental retirement plans. The \$2,000 maximum applies to all supplemental retirement plans except for the Minnesota State Colleges and Universities System (MnSCU) Higher Education Supplemental Retirement Plan, where the maximum is \$2,700. The proposed change is more than a doubling of the limit without any clear presentation of the rationale for the change and without any clear indication that the utilization of this type of supplemental retirement plan coverage is general and widespread. The proposed contribution maximum would be a 16.54 percent contribution on the average PERA-General member's covered salary (\$30,223 in 2004). Combined with the current 5.53 percent PERA-General employer contribution rate, for the tradesperson earning the average PERA-General covered salary, the total employer pension contribution load would be 22.07 percent. If the trade union contribution is a de facto member contribution, the total member pension plan contribution load at the average PERA-General covered salary would be 21.64 percent, which is a very substantial pension coverage contribution load. Any increase in this maximum can be expected to generate similar demands to increase the other Minnesota Statutes, Section 356.24, supplemental retirement plan contribution maximums.

Appendix A

Background Information on the Definition of Covered Salary for Minnesota Defined Benefit Plans

a. Defined Benefit Plans

Most Minnesota public pension plans are defined benefit plans. In defined benefit plans, the pension benefit amount that is ultimately payable is pre-determinable or fixed using a formula or comparable arrangement. The fixed element of the benefit amount leaves a variable element, which is the funding required to provide that benefit. The formula utilizes allowable service credit and salary credit in the calculation, averaging the salary amounts for the five successive years’ average salary period that produces the highest amount for use as the base to which is applied a total percentage amount determined by assigning a percentage amount to each year of allowable service credit.

b. Historical Shift to Salary-Based Plans and the Change in Salary Basis

Minnesota’s statewide retirement plans were not originally salary-related pension plans, with the predecessor to TRA established in 1915 as a money purchase (defined contribution) plan, with MSRS-General established in 1929 as a set dollar amount (\$200 per month) plan, and with PERA-General established in 1931 also as a set dollar amount (\$200 per month) plan. Conversion to salary-related pension plans occurred for MSRS-General and PERA-General in 1957, which was a recommendation of the initial interim predecessor to the Legislative Commission on Pensions and Retirement, and for TRA in 1969, which was a recommendation of the initial permanent predecessor to the Pension Commission. The first class city teacher retirement fund associations and Minneapolis Employees Retirement Fund (MERF) generally shifted to salary-related pension plans in the 1950s (the Duluth Teachers Retirement Fund Association (DTRFA) shifted in 1971).

When the statewide Minnesota retirement plans converted to salary-related pension plans, they initially utilized a “career average” salary base for determining benefits, moving to a “highest five years’ average” salary base in 1973. The career average salary utilized the salary portion of the retirement formula to account for plan members who worked in disparate compensation arrangements, either as seasonal or part-time employees or as employees with considerable overtime or extracurricular compensation, thereby not requiring sensitivity in the crediting of allowable service.

Covered salary for retirement purposes was limited for most or all public employees covered by a statewide retirement plan. In 1957, the maximum covered salary was \$4,800. In 1965, the maximum covered salary was increased to \$7,200. In 1967, covered salary was increased to a plan member’s total salary.

c. Benefit Impact of Various Employment Situations

The following demonstrates the impact of different employment situations for an MSRS-General employee (full-time employment, part-time or seasonal employment, early or late occurring mixes of part-time or seasonal employment, recurring overtime or extracurricular employment, and early or late occurring mixes of overtime or extracurricular employment), comparing career average salary and highest five years’ average salary results, including the portion of member contributions recovered by one year’s benefit amount:

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Year	Salary Increase Rate	Regular Career	Part-Time/ Seasonal Career	Early Partial Part-Time/ Seasonal Employment	Late Partial Part-Time/ Seasonal Employment	Overtime/ Extra-Curricular Career	Early Partial Overtime/ Extra-Curricular Employment	Late Partial Overtime/ Extra-Curricular Employment
1972	6.00	7,700	3,850	3,850	7,700	9,625	9,625	7,700
1973	5.95	8,162	4,081	4,081	8,162	10,203	10,203	8,162
1974	5.90	8,648	4,324	4,324	8,648	10,810	10,810	8,648
1975	5.85	9,158	4,579	4,579	9,158	11,448	11,448	9,158
1976	5.80	9,693	4,847	4,847	9,693	12,116	12,116	9,693
1977	5.75	10,256	5,128	5,128	10,256	12,820	12,820	10,256
1978	5.70	10,846	5,423	5,423	10,846	13,558	13,558	10,846
1979	5.65	11,464	5,732	5,732	11,464	14,330	14,330	11,464
1980	5.60	12,112	6,056	6,056	12,112	15,140	15,140	12,112
1981	5.55	12,790	6,395	6,395	12,790	15,988	15,988	12,790
1982	5.50	13,500	6,750	6,750	13,500	16,875	16,875	13,500

Year	Salary Increase Rate	Regular Career	Part-Time/ Seasonal Career	Early Partial Part-Time/ Seasonal Employment	Late Partial Part-Time/ Seasonal Employment	Overtime/ Extra-Curricular Career	Early Partial Overtime/ Extra-Curricular Employment	Late Partial Overtime/ Extra-Curricular Employment
1983	5.45	14,242	7,121	7,121	14,242	17,803	17,803	14,242
1984	5.40	15,018	7,509	7,509	15,018	18,773	18,773	15,018
1985	5.35	15,829	7,915	7,915	15,829	19,786	19,786	15,829
1986	5.30	16,676	8,338	8,338	16,676	20,845	20,845	16,676
1987	5.25	17,560	8,780	8,780	17,560	21,950	17,560	17,560
1988	5.20	18,482	9,241	9,241	18,482	23,103	18,482	18,482
1989	5.15	19,443	9,722	9,722	19,443	24,304	19,443	19,443
1990	5.10	20,444	10,222	10,222	20,444	25,555	20,444	20,444
1991	5.05	21,487	10,744	10,744	21,487	26,859	21,487	21,487
1992	5.00	22,561	11,281	11,281	22,561	28,201	22,561	22,561
1993	5.00	23,689	11,845	11,845	23,689	29,611	23,689	23,689
1994	5.00	24,874	12,437	12,437	24,874	31,093	24,874	24,874
1995	5.00	26,118	13,059	13,059	26,118	32,648	26,118	26,118
1996	5.00	27,423	13,712	13,712	27,423	34,279	27,423	27,423
1997	5.00	28,795	14,398	28,795	14,398	35,994	28,795	35,994
1998	5.00	30,234	15,117	30,234	15,117	37,793	30,234	37,793
1999	5.00	31,746	15,873	31,746	15,873	39,683	31,746	39,683
2000	5.00	33,333	16,667	33,333	16,667	41,666	33,333	41,666
2001	5.00	35,000	17,500	35,000	17,500	43,750	35,000	43,750
Total Member Contributions		\$22,291	\$11,146	\$14,328	\$19,109	\$27,864	\$24,052	\$23,882

	Regular Career	Part-time/ Seasonal Career	Early Partial Part-Time/ Seasonal Employment	Late Partial Part-Time/ Seasonal Employment	Overtime/ Extra-Curricular Career	Early Partial Overtime/ Extra-Curricular Employment	Late Partial Overtime/ Extra-Curricular Employment
Career Average Salary Benefit							
Career Avg. Salary	\$18,576	\$9,288	\$11,940	\$15,924	\$23,200	\$20,044	\$19,902
Benefit Accrual (0.51)	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>
Annual Ret. Benefit	\$9,474	\$4,737	\$6,089	\$8,121	\$11,842	\$10,222	\$10,150
Benefit/ Contribution Ratio	0.4250	0.4250	0.4250	0.4250	0.4250	0.4250	0.4250
High-Five Average Salary Benefit							
High-Five Avg. Salary	\$31,822	\$15,911	\$31,822	\$15,911	\$39,777	\$31,822	\$39,777
Benefit Accrual (0.51)	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>	<u>0.51</u>
Annual Ret. Benefit	\$16,229	\$8,115	\$16,229	\$8,115	\$20,286	\$16,229	\$20,286
Benefit/ Contribution Ratio	0.7281	0.7281	1.1327	0.4247	0.7280	0.6747	0.8494

d. The Purpose for Defining Covered Salary

For Minnesota defined benefit pension plans, the definition of covered salary is the measure of a plan member’s standard of living to be used in determining the appropriate replacement amount. Several decades ago, when employees received only one form of compensation as remuneration for their services, there was less question about the adequacy of using “salary” to measure a person’s standard of living. Now, with the advent of numerous employment-related compensation items, this may no longer be the case. For instance for police officers, their recurring compensation package can include a base salary, shift differential, uniform allowances, education incentive payments, court appearance amounts, dog handler compensation, tactical or special squad compensation, and overtime. There also may be additional compensation items like lump sum annual bonus or merit payments, tuition payments, and employer-paid flexible benefit account balances. Any definition or redefinition of covered salary should attempt to reasonably capture those items on which a public employee’s regular standard of living is based. Among the teacher plans, there have been recent complaints concerning the adequacy of the covered salary figure. Over the past several sessions, proposed legislation has been introduced to attempt to reflect early or mid-career extracurricular teaching compensation in the highest five successive years’ average salary figure. Also, in past legislative sessions, proposed legislation has been introduced to add an alternative highest five successive years’ average salary figure in TRA based on the average salary of all comparable TRA members, to adjust for lower salaries for some rural teachers. Similarly, the definition of covered salary should accurately reflect real compensation, so not to overstate a person’s standard of living. The late

Governor Rudy Perpich was once in the news regarding pension credit he had in the Public Employees Retirement Association (PERA) for a period of service as a Hibbing School Board member, when his salary was in dispute, when apparently there was an arrangement in Hibbing during the early and mid-1950s for school board members to rotate salaried board positions among the various members and to pair salaried and non-salaried board members in order to share the salary of one salaried position. PERA, historically, has also covered city attorneys and other professionals retained by local government units who bear a close resemblance to independent contractors and may be credited with covered salary amounts based on a gross retained fee that does not closely relate to the individual’s actual personal compensation.

e. A Comparison of Covered Salary Definitions

Over time, as compensation arrangements in public employment have become more varied and complicated, the definition of covered salary and the inclusions in it and the exclusions from it have grown. The following compares the definitions of covered salary for the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General), the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General), the Teachers Retirement Association (TRA), the Duluth Teachers Retirement Fund Association (DTRFA), the Minneapolis Teachers Retirement Fund Association (MTRFA), the St. Paul Teachers Retirement Fund Association (SPTRFA), and the Minneapolis Employees Retirement Fund (MERF):

<u>Plan</u>	<u>MSRS-General</u>	<u>PERA-General</u>	<u>TRA</u>	<u>DTRFA</u>	<u>MTRFA</u>	<u>SPTRFA</u>	<u>MERF</u>
Salary means:	(1) wages paid to an employee before deductions for deferred compensation, supplemental retirement plans, or other voluntary salary reductions; or (2) other periodic compensation, paid to an employee before deductions for deferred compensation, supplemental retirement plans, or other voluntary salary reductions; and (3) during a period of receipt of worker’s compensation while on a leave of absence, the differential between the salary that the employee would normally receive during the leave and the salary received, if any, on which the employee makes a member contribution equivalent amount. [352.01, Subds. 13 and 13a]	(1) periodic compensation before deductions for deferred compensation, supplemental retirement plans, or other voluntary salary reduction programs; (2) wages; (3) net income from fees; (4) for a member of a consolidated police or fire plan, the pre-consolidation salary rate upon which pre-consolidation member contributions were made; and (5) during a period of receipt of worker’s compensation while on a leave of absence, the differential between the salary that the employee would normally receive during the leave and the salary received, if any, on which the employee makes a member contribution equivalent amount. [353.01, Subds. 10 and 40]	periodic compensation before deduction for deferred compensation, supplemental retirement plans, or other voluntary salary reduction programs. [354.05, Subd. 35, Para. (a)]	the entire compensation paid to a teacher before deductions for deferred compensation, supplemental retirement plans, or other voluntary salary reduction programs. During a period of receipt of worker’s compensation while on a leave of absence, the differential between the salary that the employee would normally receive during the leave and the salary received, if any, on which the employee makes a member contribution equivalent amount. [354A.011, Subd. 24, Para. (a), & 354A.108]	the entire compensation paid to a teacher before deductions for deferred compensation, supplemental retirement plans, or other voluntary salary reduction programs. [354A.011, Subd. 24, Para. (a)]	the entire compensation paid to a teacher before deductions for deferred compensation, supplemental retirement plans, or other voluntary salary reduction programs. [354A.011, Subd. 24, Para. (a)]	the salary, wages, or compensation of the employee. [422A.15, Subd. 1]
Salary does not mean:	(1) lump sum sick leave payments; (2) severance payments; (3) lump sum annual leave payments; (4) overtime payments made at the time of separation from state service; (5) payments in lieu of employer-paid group insurance coverage, including the difference be-	(1) fees paid to court reporters; (2) unused annual vacation or sick leave payments, paid either in lump sum or periodically; (3) severance payments; (4) expense reimbursements; (5) lump sum settlements not attached to a specific	(1) lump sum annual leave payments; (2) lump sum wellness and sick leave payments; (3) employer-paid amounts used by an employee toward the cost of insurance coverage; (4) employer-paid fringe benefits; (5) flexible spending accounts; (6) cafeteria plans;	(1) lump sum annual leave payments; (2) lump sum wellness and sick leave payments; (3) employer-paid amounts used by an employee toward the cost of insurance coverage; (4) employer-paid fringe benefits; (5) flexible spending accounts; (6) cafeteria plans;	(1) lump sum annual leave payments; (2) lump sum wellness and sick leave payments; (3) employer-paid amounts used by an employee toward the cost of insurance coverage; (4) employer-paid fringe benefits; (5) flexible spend-	(1) lump sum annual leave payments; (2) lump sum wellness and sick leave payments; (3) employer-paid amounts used by an employee toward the cost of insurance coverage; (4) employer-paid fringe benefits; (5) flexible	

Plan	MSRS-General	PERA-General	TRA	DTRFA	MTRFA	SPTRFA	MERF
	tween single rates and family rates for an employee with single coverage; (6) employer contributions to a deferred compensation or tax-sheltered annuity program; and (7) amounts contributed under a benevolent vacation or sick leave donation program. [352.01, Subd. 13]	earnings period; (6) worker’s compensation payments; (7) employer-paid amounts used by an employee toward the cost of insurance coverage costs; (8) employer-paid fringe benefits; (9) flexible spending accounts; (10) cafeteria plans; (11) health care expense accounts; (12) daycare expenses; (13) any payments in lieu of any employer-paid group insurance coverage, including the difference between single and family rates paid to a member with single coverage; (14) certain amounts determined by the executive director to be ineligible; (15) the amount which the employing unit would otherwise pay towards single or family insurance coverage where through contract or agreement with some, but not all, employees, the employer: (i) discontinues or does not provide for new hires payment toward the cost of the employee’s selected insurance coverages under a group plan offered by the employer; (ii) makes the employee solely responsible for all contributions towards the cost of the employees selected insurance coverages under a group plan offered by the employer, including any amount the employer makes toward other employee’s selected insurance coverage under the group plan offered by the employer; and (iii) provides increased salary rates for employees who do not have any employer-paid group insurance coverages; and (16) compensation paid to volunteer ambulance personnel or volunteer firefighters unless	(7) health care expense accounts; (8) daycare expenses; (9) payments in lieu of any employer-paid group insurance coverage, including the difference between single and family rates that may be paid to a member with single coverage; (10) certain amounts determined by the executive director to be ineligible; (11) any form of payment made in lieu of any other employer-paid fringe benefit or expense; (12) any form of severance payments; (13) worker’s compensation payments; (14) disability insurance payments, including self-insurance disability payments; (15) payments to school administrators for services in addition to the normal work year contract if these services are performed on an extended duty day, a weekend, a holiday, an annual leave day, a sick leave day, or any other non-duty day; (16) severance payments under Minnesota Statutes, Section 356.24, Subd. 1, Clause (4); (17) payments made for a suspension or a leave of absence for health reasons other than accumulated sick leave under a uniform school district policy applicable equally to all similarly situated persons in the district; (18) payments made to an employee to terminate employment; (19) payments that are not clearly for the performance of services by the employee for the employer; (20) payments to a school administrator for service as an advisor or consultant to the employer under an agreement to terminate employment within two years of the execution of the agreement in an amount that is significantly different than the most recent contract salary; (21) payments under a procedure that allows the employee to designate the time of the payment if paid during the person’s formula	(7) health care expense accounts; (8) daycare expenses; (9) payments in lieu of any employer-paid group insurance coverage, including the difference between single and family rates that may be paid to a member with single coverage; (10) certain amounts determined by the executive secretary to be ineligible; (11) any form of payment made in lieu of any other employer-paid fringe benefit or expense; (12) any form of severance payments; (13) worker’s compensation payments; (14) disability insurance payments, including self-insurance disability payments; (15) payments to school administrators for services in addition to the normal work year contract if these services are performed on an extended duty day, a weekend, a holiday, an annual leave day, a sick leave day, or any other non-duty day; (16) severance payments under Minnesota Statutes, Section 356.24, Subd. 1, Clause (4), Subclause (ii); and (17) payments made for a suspension or a leave of absence for health reasons other than accumulated sick leave under a uniform school district policy applicable equally to all similarly situated persons in the district. [354A.011, Subd. 24]	ing accounts; (6) cafeteria plans; (7) health care expense accounts; (8) daycare expenses; (9) payments in lieu of any employer-paid group insurance coverage, including the difference between single and family rates that may be paid to a member with single coverage; (10) certain amounts determined by the executive director to be ineligible; (11) any form of payment made in lieu of any other employer-paid fringe benefit or expense; (12) any form of severance payments; (13) worker’s compensation payments; (14) disability insurance payments, including self-insurance disability payments; (15) payments to school administrators for services in addition to the normal work year contract if these services are performed on an extended duty day, a weekend, a holiday, an annual leave day, a sick leave day, or any other non-duty day; (16) severance payments under Minnesota Statutes, Section 356.24, Subd. 1, Clause (4), Subclause (ii); and (17) payments made for a suspension or a leave of absence for health reasons other than accumulated sick leave under a uniform school district policy applicable equally to all similarly situated persons in the district. [354A.011, Subd. 24]	spending accounts; (6) cafeteria plans; (7) health care expense accounts; (8) daycare expenses; (9) payments in lieu of any employer-paid group insurance coverage, including the difference between single and family rates that may be paid to a member with single coverage; (10) certain amounts determined by the executive director to be ineligible; (11) any form of payment made in lieu of any other employer-paid fringe benefit or expense; (12) any form of severance payments; (13) worker’s compensation payments; (14) disability insurance payments, including self-insurance disability payments; (15) payments to school administrators for services in addition to the normal work year contract if these services are performed on an extended duty day, a weekend, a holiday, an annual leave day, a sick leave day, or any other non-duty day; (16) severance payments under Minnesota Statutes, Section 356.24, Subd. 1, Clause (4), Subclause (ii); and (17) payments made for a suspension or a leave of absence for health reasons other than accumulated sick leave under a uniform school district policy applicable equally to all similarly situated persons in the district. [354A.011, Subd. 24]	

<u>Plan</u>	<u>MSRS-General</u>	<u>PERA-General</u>	<u>TRA</u>	<u>DTRFA</u>	<u>MTRFA</u>	<u>SPTRFA</u>	<u>MERF</u>
		the ambulance personnel or firefighters are plan members for that service. [353.01, Subd. 10; 353.86; 353.87]	service credit period; and (22) lump sum payments made during the employee's highest five years' salary averaging period for additional services rendered with- out pay during other years of salary. [354.05, Subds. 35 and 35a]				

Many Minnesota defined benefit public pension plans utilize a highest five successive years’ average covered salary figure for benefit calculation purposes in order to lessen the potential for manipulation from career-end compensation amounts that would occur if a shorter period of service credit was used. However, manipulation apparently occurs. It has been reported that various public employees who receive hourly compensation work substantial overtime during the period prior to retirement, in order to “boost” their highest five successive years’ average salary in plans where overtime payments are included in covered salary. Some school superintendents approaching retirement in the past have negotiated contracts that accelerated salary to the early years of the contract, during the period giving rise to the highest five successive years’ average salary, in return for an agreement to perform the superintendent’s duties for a reduced salary level (up to the Social Security earnings maximum) after retirement. The definition of covered salary must have sufficient safeguards against manipulation. In the past, there have been proposals to eliminate overtime compensation from covered salary or to set a maximum on the percentage increase in covered salary included in the highest five successive years’ average salary.

With the Combined Service Annuity provision, Minnesota Statutes, Section 356.30, there is portability of pension credit between the various Minnesota public pension plans. Portability includes the use of a common highest five successive years’ average salary for the benefit computation of all participating plans. This portability argues for consistency among the various pension plans in their definition of covered salary and the highest five successive years’ average salary. While the retirement plan administrators have argued in the past that there is substantial consistency in the salary definitions among the various pension plans, that consistency is not as clear in reviewing the comparison of various statutory definitions.