Introduction

As a resident of the State it is my/our good fortune the Commission accepts input from individuals such as myself. Meetings during the interim provide us the opportunity to present information that can be heard and reviewed prior to the busy active Legislative session. It is also encouraging that common citizens, who do not have the benefit of paid lobbyists and professional organizations speaking for them, are heard by this Committee. The path I have taken is to examine the Legislative Commission on Pensions and Retirement Principles of Pension, and present thoughts on elements of that document. These comments are essentially as that Policy applies to the Police and Fire Pension Fund. That Fund currently serves approximately ninety-five hundred retirees, and has a $1.4 billion deficit. As a retiree, goals I want the Fund to attain are balance, fairness, and self sustainability. Following is the review and comments.

Review of the Legislative Commission on Pensions and Retirement Principles of Pension Policy
2013 October 23 , by Dennis Hoelscher (Retiree, Police & Fire Pension Fund)

Preamble

The LCPR recommends the following statement of principles, which have been developed since the 1960's, 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.

Substantive Principles

Purpose of Minnesota Public Pension Plans

Item A1.

Providing, in combination with federal Social Security coverage, personal savings, and other relevant financial sources, retirement income that is adequate and affordable.

Existing retirees, in the last decade (2003-2012), received annual benefits increases that are 20% behind inflation. This is a significant deviation from the "Substantive Principle" of "providing retirement income that is adequate".

Item A 2.

Minnesota public pension plans should play their appropriate role in providing financial security to public employees in retirement.

Case above, where retirees have fallen behind inflation in the last ten years by 20%, the P & F Plan has substantially failed to meet this role. In addition the 2013 Omnibus Pension Bill, passed by the Legislature, reduced retirees previous annual pension benefit increases by 50%. At the previous rate they fell 20% behind inflation, consider what another 50% reduction will do concerning "providing financial security".

Item A 3.

As Minnesota public employees workforce trends develop, Minnesota public pension plans should be sufficiently flexible to make necessary adaptations.

"Flexible" is the key word. The current Plan needs meaningful changes, much more then the 2013 Legislature made.

What was almost totally ignored by the 2013 Omnibus Pension legislation was:

Elimination of pay to police officers for security work in private business, organizations, and private parties, when calculating initial retirement benefits.

Failure to end pension spiking.

Failure to place effective limits on initial retirement benefits.

Failure to adjust the 3% per year multiplier for calculating initial pension benefits, when for the last ten years that figure was 21% greater then inflation.

Failure to adjust the age of eligibility for full retirement benefits to reflect longer life expectancies.

Failure to enact meaningful early retirement deductions.

Failed to change the time required to be vested to something that reflects more accurately a career time period.

Structure of Minnesota Public Pension Coverage

Item 3. Consolidation of Public Pension Plans by a Minnesota Public Employer

Item 3 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.

Discussions have taken place over the years about consolidation. The LCPR interim meetings in August, 2013 were no exception. The area of "emergency and protective services" e.g. law enforcement I.e. police, sheriffs, highway patrol, conservation officers, incarceration, corrections, and security officers, fire suppression services, paramedics, and dispatch personnel – any 24 hour 365 work staffing that is directly related to emergency services - could be in a single plan.

This kind of consolidation could be cost saving in administrative and management expenditures. The shortfall has been failure to act. This could be a mandate by Commission recommendation to the Legislature.

Pension Benefit Coverage

Item 1. General Preference for Defined Benefit Plans Over Defined Contribution Plans

Item 1 b. Defined contribution plans are particularly appropriate where . . . . the defined contribution plans is a supplemental pension plan.

The current defined contribution plans, by their fiscal condition (Police and Fire a $1.4 billion deficit, and the total of plans in excess of $15 billion in deficit) indicate the current systems are not working.

Why isn't there serious consideration that something else could possibly work? Steadfastly and absolutely insisting that the defined benefit is what employees will have as a pension investment plan, denies the existence of other paths of retirement investment opportunity.

Why is it not appropriate to offer defined contribution plans as a viable option, as a replacement, or some hybrid, to the current sole defined benefit plans?

The State already provides defined contribution plans, (elected officials, city managers, ambulance service & medical personnel).

Isn't it more “democratic” that an employee be given choices, if nothing else at least for that portion the employee contributes to their pension?

Item 3. Equal Treatment Within Pension Plans

There should be equal pension treatment of public employees in terms of the relationship between benefits and contributions.

Existing retirees, in the last decade (2003-2012), received annual benefits increases that are 20% behind inflation. Comparatively, the rate used the last decade (2003-2012) to calculate initial pension benefits for current workers, has been 21% above the rate of inflation. The 41% disparity between what existing retirees receive, and what current workers will receive, certainly transgresses the principle of “equal pension treatment”.

Item 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. . . . . . .

Life expectancy has increased, and the P & F Pension Plan has a need to adapt accordingly. The existing Policy does not reflect the facts of life today. The huge federal bureaucracy of the Social Security Administration has recognized longer life expectancy and adjusted eligibility for full benefits to accommodate these facts, i.e. full retirement eligibility for those born in 1960 or later at 67.

Item 5. Appropriate Early Retirement Reductions

Public employee pension plans should not subsidize early retirement benefits . . . .

Due to minimal deductions for early retirement, coupled with essentially unlimited principal for calculating initial retirement benefits, and allowing “high five year pension spiking”, the P & F Plan in fact subsidizes early retirement. Changes made by the 2013 Omnibus Bill to “early retirement deductions” in the P & F Fund , were so nominal, they are essentially meaningless. An employee only needs to work a minimal amount of overtime during the “high five years”, to neutralize this deduction. In fact what this weak early retirement deduction does is “subsidize early retirement”

Item 7. Adequacy of Benefits at Retirement

Item 7. a. Benefit adequacy requires that retirement benefits respond to changes in the economy.

This has not happened, e.g. over the last ten years 2003-2012, future pension benefits have been calculated at a rate 21% greater then the inflation rate (future pension benefits were calculated at 3% per year, and the inflation rate has averaged just under 2.5% per year).

The initial benefits at retirement have been, and continue to be substantially above “Adequacy of Benefits at Retirement” . Conversely retirees, over the last ten years have received benefit increases 20% behind inflation. This is not only a transgression of the Policy which “requires” that retirement benefits respond to changes in the economy”, but is a significant deviation (41%) in treatment between retirees and those not yet retired.

Item 7.b. The retirement benefit should be adequate at the time of retirement.

The fact is initial retirement benefits have been in excess of adequate, because of virtually no limits at the time of retirement on the initial benefits. Causes sans “spiking”, no “ceiling”on initial benefit, allowing income derived from work that is primarily for non-governmental services, lack of meaningful early retirement deductions, etc. The Fund is being stressed by the practice of using artificially inflated principle (high five year “spiking”, and lack of a substantive “ceiling') to determine a lifetime of benefits.

Item 8. Postretirement Benefit Increases
Item 8. a. Retirement benefits should be increased during the period of retirement to offset the impact of economic inflation . . . .
In fact actions by the Legislature have done the exact opposite, e.g. over the last ten years retirees have received increases 20% less then inflation (CPI-U – all urban consumers). The rate of increases for retirees age 62 and older suffer an even greater loss against inflation, as the U.S Government rate of inflation for persons 62 year of age and older is a greater percent (CIP-E – reference person in the household is 62 years or older).

Item 19. Design of Early Retirement Incentive Programs
Item 19. b. Early Retirement incentive programs should be targeted to situations when a public employer needs to reduce staffing levels beyond normal attrition.
In fact the actions, or lack of actions, by the Legislature has the effect of encouraging early retirement without expressed need by employers. This is accomplished by having a weak early retirement deduction mechanism, as the deduction can be easily overcome by "high five year spiking" and due to the lack of ceilings on initial pension benefits.

Item 22. No Intended Ultimate Benefit Diminutions
Item 22. a. In recommending benefit plan modifications, the imposition of reductions in overall benefit coverage for existing pension plan members should not be recommended.
Because of the extraordinary Fund deficit ($1.4 billion for a plan with ninety-five hundred members) and an additional annual cash bailout of $9 million over and above what employees and employers/taxpayers pay annually, the failure to adjust initial pension benefits could cause substantial changes in benefits or the collapse of the Fund, which would be a recipe for "Benefit Diminution". There has been a substantial diminution of retirees benefits over the last decade by limiting annual increases, which has set retirees 20% behind the cost of living. It is reasonable that similar modifications be made to the benefit plan relating to plan members still working. In fact the opposite has occurred, as members working are having their future pension benefits calculated at a rate 21% greater then inflation over the last decade.

Item 22. 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.
The 2013 Legislature commenced such a program, however it is very minimal and without substance, as it was delayed a year before implementation (July 2014), and when commenced does not have effect for 33 years, or 2047. This change has no impact on today's funding deficits and merely passes the problem on to the next generation or generations. Most members of the LCPR and the Legislature will unlikely be in their positions in 33 years. Action need to be taken now, not 2, 5, 10, or 33 years down the road.

Item 22. 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.
This policy statement could be satisfied if additional changes were made that could save the pension Plan from financial collapse (which is a benefit). Changes that reduce aspects of benefit coverage can be implemented with a sunset clause, e.g. until certain funding parameters are met, I.e. 100% funding for a number of consecutive years, at which time benefits can be reviewed and changes implemented at that time which could increase benefits.

Item D. Pension Plan Funding
Item D. 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.
The current financing method for P & F pensions is vastly unfair to both current and future taxpayers. There is no fairness in the employer/taxpayer, paying minimally 50% more into the Plan, then the employee. The employee is the sole beneficiary. The fact no limits exist on initial pension benefits, calculating those benefits on a high five year basis, which include wages over and above the employees base salary (over time "spiking, and monies for essentially private security work being included as part of the base salary, using a multiplier for calculating future pension benefits that consistently is 21% higher then the Cost of Living, and an ineffective deduction for early retirement (which can be easily negated by working a minimum amount of overtime), all contribute to and in fact promote "unreasonable benefit demands".
The fact a $1.4 billion deficit exists in the Fund, and the only realistic change, by the 2013 Omnibus Pension Bill legislation, which itself has a negligible effect, and not for 33 years (as it only goes into effect for employees hired after July of 2012) was a 99% cap on initial pension benefits at the time of retirement, is ludicrous insofar as to "distribute total pension costs fairly among the current and future generations of taxpayers". Recent legislative action, or lack of, has merely kicked the can down the road, ignoring responsibilities, and pushing current problems onto future generations.

Item 3. Allocation of Funding Burden Between Members and Employers
Item 3. a. The actuarial cost of retirement benefit coverage should be financed on a shared basis between the public employee and the public employer.
This is a sound, balanced, and fair principle i.e. the employee, particularly as the sole beneficiary, should at least, match the amount paid by the employer/taxpayer. There isn't any reason this principle shouldn't be universal throughout all Plans, including the Police and Fire Plan.

Item 3. d.
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.
It is not financially sound or realistic for the employer/taxpayer to pay 50% more than the sole beneficiary, the employee. Having employers share matched equally by the employee is balanced and fair. Matching contributions is common sense and fiscally responsible.

Item 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.
Refer to the Comprehensive Annual Financial Report for the fiscal year ending June 30, 2012
Legislative Auditor Report, p. 26-07 Public Employees Police & Fire Pension Fund, overall Financial Position,
"the plans contribution rates........are deficient for the plan to become fully funded by 2039".
Doesn't this language speaks for itself!

Item G. Public Pension Plan Fiduciary Responsibility
Item G. 1. Strong Fiduciary Responsibility Standards
Public pension plan activities should be conducted in accord with strong fiduciary responsibility standards and regulation.
Doesn't a pension plan that serves a mere ninety-five hundred retirees, and has a debt of $1.4 billion, and is only 80% funded, open panoramic questions as to activities in the conduct and management of that plan meeting the standard of "strong fiduciary responsibility" ? Finger pointing is an easy diversion from accepting responsibility, particularly when it is pointed at something that is unable to respond. The "markets" are not the sole causality of Pension Fund weakness. There is a shared responsibility on actors who are both individuals and entities. This Commission has an opportunity to be a leader in recommending much needed and significant changes in moving toward fiscal responsibility.

Item G. 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.
Is it within reason that a "breach remedy" could be something as elementary as having alternative suggestions to deal with funding shortfalls be examined, through actuarial studies, and the results of those studies considered a potential basis for changes?
The PERA Board of Trustees, the Pension Commission, and the Legislature, during the 2013 Session, refused to consider suggested changes to the pension system by a group of retired police and fire fighters. These were well thought out and detailed proposals. Why is there such fear in looking outside the "box", that box being the lobbyists and representatives of organizations who represent those currently working, and not retirees? Actuarial studies of alternative proposals could be a first step toward another look at solutions.
Seven proposals were made to the Legislature in 2013, by a group essentially comprised of individuals who are currently working, and their lobbyists. Those proposals were written by these entities, presented to the PERA Board of Trustees, the Legislative Pension Commission, other Committees of the Legislature, and the Legislature as a whole. Nothing was altered from this initial proposal by these entities and these seven changes were enacted into law. The Pension Fund continues in it's state of fiscal calamity. The process by which those changes were initiated, and carried through the various bodies of government, could provide a substantial basis for cynicism by residents of this State, and reason for citizens not participating in the democratic process. Is it not time to open the windows of the Capitol and let fresh air in, and in that process help establish a financially balanced, fair, and self sustaining pension fund?

Conclusion

Currently the Police & Fire Pension Fund, which supports ninety-five hundred retirees, has a deficit of $1.4 billion. This is a huge financial shortfall. This position demands meaningful changes be made to the contribution and benefit structures. Changes are needed that more accurately reflect the economy, increased life span, current wages, and other factors. These changes are needed now, not 2, 5, 10, or 33 years down the road.

Reviewing the LCPR's "Principles of the Pension Policy" it is transparent many of the specific policy statements have been transgressed. What was specifically neglected by the 2013 Omnibus Pension Bill legislation was:
Failure to place effective limits on initial retirement benefits.
Failure to address pension spiking.
Failure to adjust the 3% per year multiplier for calculating initial pension benefits, when for the last ten years that figure was 21% greater then inflation.
Failure to adjust the age of eligibility for full retirement benefits to reflect longer life expectancies.
Failure to enact meaningful early retirement deductions.
Failure to eliminate income paid to police officers for security work in private business, organizations, and private parties, when calculating initial retirement benefits.
Failed to change the time required to be vested to something that reflects more accurately a career time period.
These elements all contribute to the fiscal burden of the pension Fund.
The singular change to the Plan that did not contribute to the fiscal burden is the bill decreased retirees pension benefit increases by 50%, i.e. from 2% down to 1%. This reduction is monumental, particularly in view of the fact retires benefits, at 2%, over the last ten years, have fallen 20% behind inflation..

According to the US Government, in June of 2013, a retiree's average yearly Social Security income was $15,228.
As of August 2013, according to the US Government, the median income, in Minnesota, for a family with a one wage earner household, was $47,122.
In January of 2013, according to the Human Resources offices of the cities of St. Paul, Minneapolis, and Hennepin County, base salaries for police and firefighters were $68,600-94,600 or more. Allowable under current legislation, by adding overtime pay, special skills pay e.g. EMT, Paramedic, HazMat, Canine Handler, Trainer SWAT, and salaries derived from essentially private security work, these base salaries, can be increased significantly.
Isn't it reasonable to conclude $68-94,000, or more, is in excess of what is "adequate" and "affordable", and a major diversion from "Substantive Principles"?

For those still working, future retirement benefits are being calculated at a rate 21% greater then the inflation rate for the last decade (2003 to 2012). This continued practice in itself is "inflationary" and damaging to a fund in financial crisis. At the same time the annual rate of increases for existing retirees, over that same decade, was 20% less then the inflation rate. This is antithetical to retirees receiving "retirement income that is adequate". Retirees benefits have not been "increased during the period of retirement to offset the impact of economic inflation" (Reference II Substantive Principles A. Purpose of Minnesota Public Pension Plans Item 1. - - "Retirement benefits should be increased during the period of retirement to offset the impact of economic inflation . . .. ") but have been in fact diminished. Unlimited initial pension benefits are allowed, at the expense of retirees annual increases. This is not a fair or balanced system.

It is hoped the direction of the LCPR, in discussing "Pension Policy" during interim meetings, is not to simply "justify" actions which are out of compliance with existing Policy. The hope is discussion will lead to changes that are balanced, fair, and effective in dealing with funding shortfalls. Wouldn't it be prudent and fair for the Commission to have actuarial studies of alternative proposals, and the results of those studies be open for public discussion?
The Commission has exercised wide discretion under the Policy as to "public pension plans should be sufficiently flexible to make necessary adaptations". A balanced, fair, and self sustaining Fund requires meaningful adjustments to the Pension Fund. The time is now to rethink the current financial status of the Police & Fire Fund, and to take actions toward building financial stability, which is not on the backs of retirees or taxpayers.

During the last Legislative Session retirees presented proposals to help alleviate the financial condition of the Police & Fire Pension Fund. The goals of those proposals were a balanced, fair, and self sustaining fund. They did not rely on surcharges, annual cash bailouts by taxpayers. In fact they reduced burdens on employers/taxpayers. Alternative proposals, to the 2013 Omnibus Pension Bill legislation deserve to be heard. They could have great value in helping establish fiscal stability of the P & F Pension Fund.