State of Minnesota \ LEGISLATIVE COMMISSION ON PENSIONS AND RETIREMENT

H.F. 565	**S.F. 519**
(O'Driscoll)	(Pappas)

Executive Summary of Commission Staff Materials

Affected Pension Plan(s): Statewide and major local retirement plans

Relevant Provisions of Law: Minnesota Statutes, Section 354A.29; 356.415

General Nature of Proposal: Financial sustainability triggers for the return to full post-retirement adjustment rates

Date of Summary: February 27, 2015

Specific Proposed Changes

- Increase in minimum receipt period for adjustment qualification.
- Reduction in minimum receipt period for adjustment qualification.
- Trigger for future financial sustainability loss reduced adjustment rate.
- Elimination of Consumer Price Index post-retirement adjustment mechanism.

Policy Issues Raised by the Proposed Legislation

General Issues:

1. Appropriateness of continuing post-retirement adjustment mechanisms not based on any inflation measure.
2. Appropriateness of the current and proposed lack of uniformity in post-retirement adjustment mechanisms.
3. Continuing ramifications of basing post-retirement adjustment rates on funding levels.
4. Appropriate asset value for actuarial work and post-retirement adjustment triggers.

Specific Issues:

5. Appropriateness of an increase in the minimum waiting period for an initial partial post-retirement adjustment.
6. Appropriateness of a decrease in the minimum waiting period for an initial partial post-retirement adjustment.
7. Appropriateness of adding a reduced rate post-retirement adjustment trigger for a future loss of financial sustainability.
8. Remaining potential for yo-yoing in post-retirement adjustment rates in the current reduction triggers.
9. Appropriateness of the elimination of the CPI-based post-retirement adjustment mechanism for PERA-P&F.

Potential Amendments

H0565-1A implements the use of the market value of assets instead of the actuarial value of assets in retirement plan actuarial reporting.

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TO:	Members of the Legislative Commission on Pensions and Retirement
FROM:	Lawrence A. Martin, Executive Director
RE:	H.F. 565 (O'Driscoll); S.F. 519 (Pappas): Statewide and Major Local Retirement Plans; Modification in Financial Sustainability Triggers for the Return to Full Post-Retirement Adjustment Rates
DATE:	February 26, 2015

General Summary of H.F. 565 (O'Driscoll); S.F. 519 (Pappas)

H.F. 565 (O'Driscoll); S.F. 519 (Pappas) amends Minnesota Statutes, Sections 354A.29 and 356.415, the St. Paul Teachers Retirement Fund Association and many statewide retirement plan post-retirement adjustment provisions, by making the following changes in the post-retirement adjustment mechanisms:

1. Increase in Minimum Receipt Period for Adjustment Qualification. The current three-month period of minimum benefit receipt to qualify for the initial post-retirement adjustment is increased to six months for the St. Paul Teachers Retirement Fund Association (SPTRFA) (Sec. 1-3);

2. Reduction in Minimum Receipt Period for Adjustment Qualification. The current six-month period of minimum benefit receipt to qualify for the initial post-retirement adjustment is reduced to one month for the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General), the Correctional State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-Correctional), the Legislators/Constitutional Officers Retirement Plan, the State Patrol Retirement Plan, the Judges Retirement Plan, and the Teachers Retirement Association (TRA) (Sec. 5, 7-9);

3. Trigger for Future Financial Sustainability Loss Reduced Adjustment Rate. If financial stability is restored, the post-retirement adjustment rate will again be reduced if the market value of retirement plan assets funded ratio (asset value as percentage of actuarial accrued liabilities) declines for MSRS-General, MSRS-Correctional, Legislators/Constitutional Officers Plan, and TRA (85% for two years; 80% for one year), and for the SPTRFA (90% for two years with 2% rate; 80% for two years with 1% rate) (Sec. 2-3, 5, 7-8); and

4. Elimination of Consumer Price Index Post-Retirement Adjustment Mechanism. The current, but un-implemented, post-retirement adjustment mechanism based on the Consumer Price Index increase, up to 2.5% annually, was eliminated and replaced by a flat 2.5% adjustment rate for PERA-P&F (Sec. 6).

Detailed Summary of H.F. 565 (O'Driscoll); S.F. 519 (Pappas)

A detailed summary of H.F. 565 (O'Driscoll); S.F. 519 (Pappas) is attached.

Background Information

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

- **Attachment A**: Comparison of the Current Post-Retirement Adjustment Mechanisms for Retirees, Disabilitants, and Survivors.
- **Attachment B**: Background Information on Minnesota Public Employee Defined Benefit Retirement Plan Post-Retirement Adjustment Mechanisms.
- **Attachment B**: Background Information on the Actuarial Value of Public Pension Plan Assets.

Discussion and Analysis

H.F. 565 (O'Driscoll); S.F. 519 (Pappas) revises the reduced rate post-retirement adjustment mechanisms of many statewide retirement plans (all but the General Employee Retirement Plan of the Public Employees Retirement Association (PERA-General) and the Local Government Correctional Service Retirement Plan (PERA-Correctional)) and the post-retirement adjustment mechanism of the St. Paul Teachers Retirement Fund Association (SPTRFA), by increasing the minimum receipt period required to qualify for an SPTRFA post-retirement adjustment, by reducing the minimum receipt period required to qualify for a post-retirement adjustment for most of the statewide retirement plans, by providing for a future post-retirement adjustment reduced rate if funded ratios fall below the current law rate restoration triggers for the plans administered by the Minnesota State Retirement System (MSRS), for the Teachers Retirement Association (TRA), and for the St. Paul Teachers Retirement Fund Association (SPTRFA), and by eliminating the Consumer Price Index-based post-retirement adjustment mechanism currently applicable, but never implemented by, the Public Employees Police and Fire Retirement Plan (PERA-P&F).

The proposed legislation raises a number of pension and related public policy issues for Commission member consideration and possible discussion, including the following:

General Issues

1. Appropriateness of Continuing Post-Retirement Adjustment Mechanisms Not Based on Any Inflation Measure. The policy issue is the appropriateness of continuing the practice of utilizing post-retirement adjustment mechanisms that are not clearly based in amount on any measure of inflation. Principle II.C.8. of the Commission's Principles of Pension Policy provides, in part, that

   > [R]etirement benefits should be increased during the period of retirement to offset the impact of economic inflation over time in order to maintain a retirement benefit that was adequate at the time of retirement.

   That principle builds on Principle II.C.7., which indicates that retirement benefits should be adequate, implicitly rather than explicitly defined, at the time of retirement. Together, the principles provide that the goal of Minnesota's public pension plan coverage should be benefits that are adequate when they commence and that are protected from becoming less than adequate from inflation during the course of benefit receipt. However, only two Minnesota defined benefit public employee retirement plans currently have any connection to any inflation measure in setting the adjustment amount. Under current law, upon regaining financial sustainability, the Public Employees Police and Fire Retirement Plan (PERA-P&F) would provide a rate of increase equal to the annual percentage increase in the federal Consumer Price Index (June 30 to June 30) up to 2.5% annually. Under current law, upon regaining financial sustainability, the St. Paul Teachers Retirement Fund Association (SPTRFA) would provide a rate of increase equal to the annual percentage increase in the federal Consumer Price Index (average third-quarter to average third-quarter) up to 5%. Between 1992 and 2009, the joint post-retirement adjustment mechanism for the statewide defined benefit public employee retirement plans, the Minnesota Post Retirement Investment Fund, included a cost-of-living adjustment component, based on the annual percentage increase in the federal Consumer Price Index, up to 3.5% annually initially, and up to 2.5% annually after 1997, but that basis for adjustments was proposed by the statewide retirement plan administrators for elimination in 2009 when the Minnesota Post Retirement Investment Fund was dissolved and the Commission included the change in the 2009 Omnibus Retirement Bill. Currently, post-retirement adjustments for most retirement plans are a flat-rate annual increase, without regard to any measure of inflation measure. If the public employee retirement plan does not provide post-retirement adjustments with some basis in a measure of inflationary impacts on retiree fixed incomes, as is the case with most Minnesota public employee pension plans, it is very difficult to identify the public policy rationale underlying the mechanism and it will be very difficult for the Commission to process future proposed modifications in the current mechanisms other than considering actuarial cost impacts.

2. Appropriateness of the Current and Proposed Lack of Uniformity in Post-Retirement Adjustment Mechanisms. The policy issue is the current level of dissimilarity between the various defined benefit statewide and major local retirement plans with respect to their post-retirement adjustment mechanisms and the increase in dissimilarity being advocated by the various retirement plan administrators in the proposed legislation. Principle II.C.6. of the Commission's Principles of Pension Policy provides that

   > [T]here 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.

   Attachment A is a comparison of the features of the current post-retirement adjustment mechanisms for the ten remaining statewide and major local retirement plans (plus the MERF Division of PERA and the Duluth Teachers Retirement Fund Association (DTRFA), both of which recently merged with another retirement plan) and the comparison indicates a fair degree of dissimilarity. The proposed legislation has some similarities (ongoing loss of financial sustainability adjustment rate downsizings added where they previously did not exist), but also includes further dissimilarities. The current and likely future lack of uniformity does not appear to be based on plan demographics, retirement coverage, or member contributions. The Commission should consider requesting from the various retirement plan administrators a clear statement of the pension public policy rationale of the current and additional degree of non-uniformity, in the mechanisms and why a more uniform approach to post-retirement adjustments would be ill advised.

3. Continuing Ramifications of Basing Post-Retirement Adjustment Rates on Funding Levels. The policy issue, which arose with the 2010 post-retirement adjustment modifications and continues with these post-retirement adjustment mechanism suggested revisions, is the appropriateness of basing post-retirement adjustment amounts on retirement plan funded ratios. In suggesting that retirees bear some portion of the impact of benefit modifications needed to address a presumed once-in-a-lifetime economic disaster, a temporary reduction in post-retirement adjustment rates was the appropriate (actually the only feasible) vehicle. The tying of the post-retirement adjustment rate reductions to a retirement plan funded ratio and setting the trigger for the restoration of the pre-2010 post-retirement adjustment rates based on the attainment of a particular funded ratio may represent the inertia of the argument used by the plan administrators to attain buy-in by the retirees for the reduction rather than sound public policy and adding permanent triggers for future automatic post-retirement adjustment rate reductions as contained in the proposed legislation further ties funding issues with benefit provision issues. One of the policy deficiencies with the pre-2009 Minnesota Post Retirement Investment Fund was its link of post-retirement adjustments to pension funding developments, primarily the reliance on one actuarial experience gain item to fund post-retirement adjustments. Based on the link that is being established between funding and post-retirement adjustment levels, past legislation and this proposed legislation is setting the stage for arguments by retirees for symmetrical post-retirement adjustment enhancements whenever Minnesota statewide and major local retirement plans become well-funded again. The first retirement plan when this may occur is the Local Government Correctional Service Retirement Plan (PERA-Correctional), which was the first plan to trigger a return to the pre-2010 post-retirement adjustment rate and appears to be on track to be fully funded in the near term. While setting benefits with an eye to affordability is sensible public policy, the tie between plan funding health and benefit levels should not be made so clear and automatic that it provides an argument for future benefit increase proposals solely because of the impact of bull investment markets for a few years.

4. Appropriate Asset Value for Actuarial Work and Post-Retirement Adjustment Triggers. The policy issue is the difference between the value of assets used for actuarial valuation preparations and other actuarial purposes and the asset value used for the post-retirement adjustment mechanism trigger for the restoration of the pre-2010 adjustment rate. For most purposes, the actuarial value of assets is used. For the post-retirement adjustment mechanism trigger, the market value of assets is used. As it suits their argument, including the preparation of actuarial cost estimates of potential legislation that they suggest, the fund administrators choose between the two. The actuarial value of assets is a five-year smoothing of the difference between the market value of assets and the expected change in value using the applicable actuarial assumptions. The market value of assets is the single-date (fiscal year end) value used in the audited financial reporting of the retirement plan. The actuarial value of assets, because of its smoothing effect, delays the recognition of the full impact of investment market changes. The shift from the 1984 calculated value of assets that occurred in 2000 was a recommendation of the primary consultant of the actuarial consulting firm retained by the Commission at that time, Milliman & Robertson, Inc. Milliman recommended the change, as the Commission staff remembers the discussion, in order to minimize or eliminate short-term market volatility from the actuarial work and to insulate the investment management of a retirement plan from adverse pressure to rebalance investment portfolios or other investment mix or selection changes that result in an investment loss over the short run. Since Minnesota defined benefit retirement plans utilize both values, generally favoring market value in recent years, since the State Board of Investment appears to be largely or wholly immune to pressure to postpone or decline to make investment changes it otherwise would, and since using the differing asset values and the consequent actuarial results that each produce makes communicating information about Minnesota pension plan financial and funding conditions more difficult, serious consideration should be given by the Commission to settling on a single value of assets for actuarial reporting, the market value of assets. The following compares the actuarial value of assets and the market value of assets for the various statewide and major local retirement plans for 2014, where the market value of assets trends about 1% higher than the actuarial value of assets, and the differing funded ratios under each:

		Actuarial Value		Market Value	
Retirement Plan	Actuarial Accrued Liability	Actuarial Value of Assets	Actuarial Value Funded Ratio	Market Value of Assets	Market Value Funded Ratio
MSRS-General	$12,445,126,000	$10,326,272,000	82.97%	$11,498,604,000	92.41%
PERA-General	$21,282,504,000	$15,644,540,000	73.51	17,404,822,000	81.78
TRA	$24,528,506,000	$18,181,932,000	74.10	20,289,594,000	82.70
MSRS-Correctional	$1,122,474,000	$790,304,000	70.41	877,056,000	78.14
State Patrol	$800,421,000	$597,870,000	74.69	667,340,000	83.37
PERA-P&F	$8,151,328,000	$6,525,019,000	80.05	7,273,100,000	89.23
PERA-Correctional	$426,506,000	$410,489,000	96.24	453,232,000	106.27
Judges	$298,233,000	$157,528,000	52.82	175,556,000	58.87
SPTRFA	$1,533,603,000	$8,947,972,000	61.81	1,045,400,000	68.17

- **Amendment H0565-1A** amends Minnesota Statutes, Section 356.215, Subdivision 1, to implement the use of market value of assets instead of the actuarial value of assets in retirement plan actuarial reporting.

Specific Issues

5. Appropriateness of an Increase in the Minimum Waiting Period for an Initial Partial Post-Retirement Adjustment. The policy issue is whether or not it is appropriate to increase the minimum period of annuity or benefit receipt to become eligible for a partial post-retirement adjustment during the initial year of annuity or benefit receipt. The St. Paul Teachers Retirement Fund Association (SPTRFA), in sections 2 and 3 of the bill, is proposing changing the current minimum receipt requirement of three months to six months and changing the partial initial post-retirement adjustment from a proration on the basis of the number of calendar quarters of receipt to a flat 50% reduction. The current minimum receipt requirement for the various statewide retirement plans until financial sustainability (market value of assets equal or exceed either 85% or 90% of actuarial accrued liabilities) is restored is six months. Since most active teachers are likely to retire at the end of a school year, the minimum receipt period and change in partial adjustment reduction amount is unlikely to have much impact beyond deferred retirees and inactive members who become eligible for a retirement annuity in the future under a portability mechanism, where an April 1 retirement would produce a half benefit amount rather than a three-quarters benefit amount, and an October 1 retirement would lose all eligibility for the next post-retirement adjustment. The Commission should consider requesting a clear statement of its intent in and the policy basis for adding these restrictions.

6. Appropriateness of a Decrease in the Minimum Waiting Period for an Initial Partial Post-Retirement Adjustment. The policy issue is whether or not it is appropriate to reduce the minimum period of annuity or benefit receipt to become eligible for a partial post-retirement adjustment during the initial year of annuity or benefit receipt. The change from requiring six months receipt to one month receipt is being proposed for all of the statewide public employee defined benefit retirement plans except for the Public Employees Police and Fire Retirement Plan (PERA-P&F), which sought and received the reduction for pre-June 2, 2014, retirees and increased the minimum annuity receipt period to 25 months for post-June 1, 2014, retirees in 2014, and except the General Employee Retirement Plan of the Public Employees Retirement Association (PERA-General) and the Local Government Correctional Service Retirement Plan (PERA-Correctional), which sought and received the reduction for all future retirees in 2014. The imposition of a minimum receipt requirement beyond one month was imposed in 2010 for the statewide retirement plans for the duration until financial sustainability is restored as an actuarial cost savings item. Only PERA-Correctional has regained financial sustainability after 2010, but the various statewide plans are seeking this relaxation of a cost saving element despite remaining financially impaired based on their market value of assets funded ratio measure. The financial argument for the PERA-General and PERA-Correctional change in 2014 was not explicitly made to the Commission by PERA. The Commission may wish to explore the policy rationale for this relaxation at this time with MSRS and TRA and may wish to consider the policy disjunction of significantly increasing the minimum receipt requirement for post-June 1, 2014, PERA-P&F retirements, modestly increasing the minimum receipt requirement for post-June 30, 2015, SPTRFA retirements, and reducing the minimum receipt requirement for all other retirement plans between 2014 and this proposed legislation.

7. Appropriateness of Adding a Reduced Rate Post-Retirement Adjustment Trigger for a Future Loss of Financial Sustainability. The policy issue is the appropriateness of adding to the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General), the MSRS Correctional State Employees Retirement Plan (MSRS-Correctional), the State Patrol Retirement Plan, the Teachers Retirement Association (TRA), and the St. Paul Teachers Retirement Fund Association (SPTRFA) an extension to the 2010 post-retirement rate reduction to apply if there is another situation in the future where the funded ratio of the retirement plan falls below 85% or 90% for one or two consecutive actuarial valuations. In 2010, as part of the financial sustainability legislation promoted by the statewide retirement plan administrations, the PERA-administered plans crafted their post-retirement adjustment rate reduction provisions to apply to both 2010 and to any future significant drop in funded ratio measured on a market value of assets basis, but the other retirement plans administrations did not follow suit even though the differential in treatment was pointed out in the Commission staff issue memorandum presented at that time. Now they are proposing the same change five legislative sessions later, MSRS and TRA must have changed their mind in the interval and the Commission may wish to explore what problems the retirement plan administrations see in the future now that they did not see in 2010 and that causes them concern.

8. Remaining Potential for Yo-Yoing in Post-Retirement Adjustment Rates in the Current Reduction Triggers. The policy issue is whether the ongoing automatic provisions that will reduce the post-retirement reduction rates in the event of a significant decline in a retirement plan's funded ratio measured on a market value of assets basis could function inappropriately, causing a yo-yoing in post-retirement adjustment rates back and forth every few years. This issue was raised in the 2010 financial sustainability legislation Commission staff issue memorandum with respect to the PERA-administered retirement plan provisions, but not addressed at all by PERA until 2013, when the Local Government Correctional Service Retirement Plan (PERA-Correctional) neared reclaiming financial sustainability. The potential yo-yoing was addressed by PERA by broadening the trigger to cover two actuarial valuations, which has been replicated by the various statewide retirement plan administrators and the St. Paul Teachers Retirement Fund Association (SPTRFA). The yo-yoing occurs because a reduction in the applicable post-retirement rate for a retirement plan with a significant number of retirees will potentially release a considerable amount of actuarial accrued liability when implemented, which in turn will greatly improve the retirement plan's funded ratio if no other significant generator of actuarial accrued liability significantly deviates from the applicable actuarial assumptions. That significant increase in the plan's funded ratio from the post-retirement adjustment rate reduction makes the implementation of the trigger to return to the full post-retirement adjustment more likely in the short run if there are even modest actuarial experience gains in investment performance, salary increase rates, or mortality. While the two-year actuarial valuation results addition to the trigger mechanism could lengthen the period between bouncing back and forth between the reduced post-retirement adjustment rate and the full post-retirement adjustment rate, it still does not eliminate the mindless automatic operation of the underlying trigger. To demonstrate this, consider if one of the statewide retirement plans is 91% funded on a market value of assets basis in fiscal year A, falls to 85% funded on a market value of assets basis because of an investment market dip in fiscal years B and C, triggering an automatic reduction in the post-retirement adjustment rate in mid-fiscal year D, which releases a fair amount of retiree actuarial accrued liability recognized at the end of fiscal year D, increasing the plan's funded ratio again, which if combined with active member salary freezes or other experience gains that frequently accompany state budgetary problems caused by an economic recession in fiscal years E and F, could result in a return to the full post-retirement adjustment rate for mid-fiscal year G, which when recognized at fiscal year G end, will again significantly impact the funded ratio, potentially starting the cycle all over. Since the economy has many moving parts and the pension plan liabilities and funding are dynamic, utilizing automatic triggers that affect the benefits paid to individuals on fixed incomes in retirement without any discretion could lead to a roller coaster ride in post-retirement adjustment rates over the medium or the long term.

9. Appropriateness of the Elimination of the CPI-Based Post-Retirement Adjustment Mechanism for PERA-P&F. The policy issue is whether or not it is appropriate to eliminate the post-retirement adjustment mechanism based on the annual percentage increases in the federal Consumer Price Index (CPI) that currently applies to the Public Employees Police and Fire Retirement Plan (PERA-P&F) when the financial sustainability of that plan is restored. The elimination of the PERA-P&F CPI-based p post-retirement adjustment mechanism is proposed by PERA. The mechanism had been enacted in 2010 at the request of representatives of statewide public safety organizations as an alternative to the post-retirement adjustment modifications proposed jointly by the statewide retirement plan administrations. As noted in issue #1 above, a CPI-based post-retirement adjustment mechanism is more consistent with the Commission's Principles of Pension Policy than the mechanisms enacted in 2009 and modified in 2010. Since the current, but unimplemented, PERA-P&F CPI-based post-retirement adjustment mechanism was formulated and advanced by the statewide public safety organizations, the Commission may wish to take testimony specifically from those statewide public safety employee groups on the topic before acting on the PERA request for its elimination.

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Detailed Summary of H.F. 565 (O'Driscoll); S.F. 519 (Pappas)

The proposed legislation makes the following changes for the retirement plans indicated:

1) General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General). The reduced post-retirement adjustment rate would be triggered in a future loss of financial sustainability once the current loss of financial sustainability is reversed upon the market value of assets funding ratio falling below 85% for two actuarial valuations or below 80% for the most recent actuarial valuation and the current six-month minimum benefit receipt period is reduced to one month for initial post-financial-sustainability-loss reduced rate post-retirement adjustments (Sec. 5).

2) MSRS Correctional State Employees Retirement Plan (MSRS-Correctional). Same as MSRS-General (Sec. 5).

3) Legislators/Constitutional Officers Retirement Plan. Same as MSRS-General, based on MSRS-General market value of assets funding ratio (Sec. 5).

4) State Patrol Retirement Plan. The reduced post-retirement adjustment rate would be triggered in a future loss of financial sustainability once the current loss of financial sustainability is reversed upon the market value of assets funding ratio falling below 80% for two actuarial valuations or below 75% for the most recent actuarial valuation and the current six-month minimum benefit receipt period is reduced to one month for initial reduced rate post-financial-sustainability-loss reduced rate post-retirement adjustments (Sec. 8).

5) Judges Retirement Plan. The current six-month minimum benefit receipt period for the initial reduced rate post-financial sustainability loss post-retirement adjustment payment is reduced to one month (Sec. 9).

6) Public Employees Police and Fire Retirement Plan (PERA-P&F). The payment of post-retirement adjustments based on the increase in the Consumer Price Index, up to 2.5%, once financial sustainability is regained is replaced with a flat rate 2.5% adjustment (Sec. 6).

7) Teachers Retirement Association (TRA). The reduced post-retirement adjustment rate would be triggered in a future reversal of financial sustainability once the market value of assets funding ratio falling below 85% for two actuarial valuations or below 80% for the most recent actuarial valuation and the current six-month minimum benefit receipt period for the initial reduced rate post-financial-sustainability-loss post-retirement adjustment payment is reduced to one month (Sec. 8).

8) All Statewide Plans. The calculations of the partial post-retirement adjustment rate with initial benefit receipt of less than a full year once financial sustainability is restored is clarified to eliminate a possible interpretation of an increase greater than 12/12ths (Sec. 4).

9) St. Paul Teachers Retirement Fund Association (SPTRFA). The minimum period of annuity or benefit receipt required to receive the initial post-retirement adjustment is increased from three months to six months (Sec. 1-3) and a reduced post-retirement adjustment rate would be triggered in a future loss of financial sustainability once the current loss of financial sustainability is reversed upon the market value of assets funding ratio falling below 90% (2% rate) or below 80% (1% rate) for two consecutive actuarial valuations (Sec. 2-3).

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Comparison of the Current Post-Retirement Adjustment Mechanisms for Retirees, Disabilitants, and Survivors

	MSRS-General, MSRS-Correctional, Legislators/ Elected State Officers	Judges Plan	State Patrol Plan	PERA-General PERA-Correctional	PERA-P&F	TRA	SPTRFA	DTRFA
Definition of Funding Stability:	One trigger: 90% funded MVA* in two consecutive valuations *(Note: Legislators/ESO will use MSRS-General funding ratio)*	Two triggers: a) up to 70% funded MVA* in two prior consecutive valuations b) 70% up to 90% funded in two prior consecutive valuations Full adjustment upon 90% funding	Two triggers: a) up to 85% funded MVA* in two consecutive valuations b) 85% up to 90% funded in two consecutive valuations Full adjustment upon 90% funding	Permanent requirement: 90% funded on MVA* in 2 consecutive valuations Reduced adjustments recur if MVA funding ratio falls below 85% in 2 consecutive valuations or below 80% in one	Permanent requirement: 90% funded on MVA* in 2 consecutive valuations Reduced adjustments recur if MVA funding ratio falls below 85% in 2 consecutive valuations or below 80% in one	One trigger: At least 90% funded MVA* in two most recent valuations	Two standards until 90% funding ratio achieved: a) up to 80% funded AVA^ in two most recent valuations b) 80% up to 90% funded in two most recent valuations Upon 90% funding, re-pealed and replaced by inflation match up to 5%	One trigger followed by blink-off inflation match: a) 1% adjustment paid until 90% funded AVA^ Upon 90% funding, re-placed by inflation match up to 5% but no adjustment paid if funding ratio falls below 80%
If funding stability is not achieved:								
Minimum period in benefit receipt for full adjustment	18 months	18 months	18 months	12 months	In benefit receipt: Before 6/2/14: 12 mo. After 6/1/14: 36 mo.	18 months	12 months	12 months
Full adjustment	2.0%	a) up to 70% MVA 1.5% b) 70% up to 90% 2.0%	a) up to 70% MVA 1.5% b) 70% up to 90% 2.0%	1.0%	1.0%	2.0%	a) up to 80% AVA: 1.0% b) 80-89% AVA: 2.0%	1.0%
Minimum period in benefit receipt for prorated adjustment	6 months	6 months	6 months	1 month	In benefit receipt: Before 6/2/14: 1 mo. After 6/1/14: 25 mo.	6 months	3 months	N/A
Prorated adjustment	For months 6-18: 1/12th of full adjustment for each month	For months 6-18: 1/12th of applicable full adjustment rate for each month	For months 6-18: 1/12th of applicable full adjustment rate for each month	For months 1-12: 1/12th of full adjustment for each month	For months 1-12/25-36 as applicable: 1/12th of full ad-justment for each mo.	For months 6-18: 1/12th of full adjustment for each month	Applicable rate prorated by whole calendar year quarters in benefit receipt	N/A
If funding stability is achieved:								
Minimum period in benefit receipt for full adjustment	12 months	12 months	12 months	12 months	36 months	12 months	12 months	12 months
Full adjustment	2.5%	2.5%	2.5%	2.5%	Inflation match not to exceed 2.5%	2.5%	Inflation match not to exceed 5%	Inflation match not to exceed 5% unless annual funding rate is under 80%
Minimum period in benefit receipt for prorated adjustment	1 month	1 month	1 month	1 month	25 months	1 month	3 months	3 months
Prorated adjustment	For months 1-12: 1/12th of full adjustment for each month	For months 1-12: 1/12th of full adjustment for each month	For months 1-12: 1/12th of full adjustment for each month	For months 1-12: 1/12th of full adjustment for each month	For months 25-36: 1/12th of full adjustment for each month	For months 1-12: 1/12th of full adjustment for each month	Full adjustment prorated by whole calendar year quarters in benefit receipt	Full adjustment prorated by whole calendar year quarters in benefit receipt

**MVA = Market value of assets basis ^AVA = Actuarial value of assets basis*

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Background Information on
Minnesota Public Employee Defined Benefit Retirement Plan
Post-Retirement Adjustment Mechanisms

1. Purpose of Post-Retirement Adjustments. In the early years of the Commission, the 1950s and early 1960s, the Commission's Principles of Pension Policy lacked a coherent post-retirement adjustment policy statement. These early principles statements recognized the need to occasionally adjust retiree benefits to alleviate harm, but principles statements reflected fear of creating any systematic post-retirement adjustment provisions due to concern about the accompanying liabilities and their impact on plan financing. According to these early documents, post-retirement benefit adjustments ought to be ad hoc, should be considered as a gratuity or as assistance rather than a pension right, and should be financed outside of the pension funds. For example, the 1961 version of the Principles of Pension Policy reads *"Raises in pension benefits to retired persons should be recognized as a form of assistance and not disguised as pensions. Such grants should in all instances be separately financed and never charged to the pension funds."*

   This statement remained unchanged in substance through the 1973 version of the Commission's Principles of Pension Policy statement, and possibly later. But by 1977, the post-retirement policy stated in the principles document had been fully transformed. Instead of calling for occasional ad hoc adjustments, without prefunding and financed outside of the pension funds, the 1977-78 version of the policy document states that the retirement benefit of a long term employee should be adequate at the time of retirement and those benefits should be kept adequate during retirement by systematic increases necessary to maintain purchasing power. Specifically, the document states *"The retirement benefit should be adequate during the period of retirement. There should be a system of prefunded periodic post-retirement increases. Where possible, post-retirement adjustments should follow some valid recognized economic indicators."*

   More recent versions of the policy document reflect the same policy, but are more specific in the necessary requirements. For example, the Commission's most recent Principles of Pension Policy document (in Principle II.C.8.) regarding post-retirement increases states *"Retirement benefits should be increased during the period of retirement to offset the impact of economic inflation over time in order to maintain a retirement benefit that was adequate at the time of retirement. The system of periodic post-retirement increases should be funded on an actuarial basis."*

   From the late 1970s through the most recent document, the Commission's policy document reflects a mindset that 1) post-retirement adjustments are an integral component of the pension earned by the employee over his or her working career in public service, rather than an added gratuity or a form of charity; 2) adjustments ought to match inflation; and 3) adjustments should be funded on an actuarial basis.

   If a benefit is adequate at the time of retirement but adjustments exceed inflation, the adjustments are excessive. Similarly, if the adjustments are insufficient to offset inflation, the value of the benefit in real terms erodes over time, causing a benefit that was adequate at retirement to become inadequate in later years. Furthermore, since post-retirement adjustments are an integral component of the pension, rather than a gratuity, and these adjustments are funded on an actuarial basis, it is reasonable and appropriate to finance them through the pension funds. That financing practice has become the norm.

2. History of Minnesota Post-Retirement Adjustments. This section provides an historical overview of the primary procedures used to adjust pensions during the period of benefit receipt. These are generally referred to as "post-retirement" adjustments, but some individuals receiving adjustments may not be retired. At least in more recent times, any adjustments after benefits commence are provided not only to retired public employees, but also to plan disabilitants and survivors. Unless otherwise stated, in this memo references to benefit adjustments for retirees apply to retired employees, disabled employees, and survivors who receive annuities under the applicable plan or plans.

   First reviewed are procedures used by the two remaining first class city teacher retirement fund associations, the Duluth Teachers Retirement Fund Association (DTRFA) and the St. Paul Teachers Retirement Fund Association (SPTRFA), followed by a review of the plans invested through the State Board of Investment (SBI), which are the Minnesota State Retirement System (MSRS), the Public Employees Retirement Association (PERA), and the Teachers Retirement Association (TRA).

Before beginning that review, a listing of the types of adjustments which have been used in the Minnesota public plans covered by this memo may be helpful. These are:

- Ad hoc adjustments. In the distant past, the only post-retirement adjustments provided were occasional ad hoc adjustments.
- Thirteenth check. The 13th check, used for several years by the DTRFA and SPTRFA, is an additional check paid to benefit recipients, financed by the liquation of some small portion of a plan's pension assets. Depending on specific requirements in law, a distribution could occur every year, or some specified level of investment return or investment income could be used to trigger a distribution. The total amount available for distribution could be distributed in equal amounts to eligible recipients, or weighted toward those with the most service credit, or weighted by years in retirement, or by a combination of years of service credit and years in retirement. These amounts were not added to the pension base for purposes of computing subsequent benefit amounts.
- Fixed percentage adjustment plus an excess investment return related percentage adjustment. This approach has been used by first class city teacher plans.
- Percentage adjustments which escalate with the plan's funding ratio.
- Inflation match adjustments up to a cap, plus possible percentage adjustments based on excess reserves. The former Minnesota Post Retirement Investment Fund is an example.
- Inflation match or a capped inflation match.

a. Duluth Teachers Retirement Fund Association (DTRFA) Adjustments.

1) Ad Hoc Adjustments. In the 1960s through 1981, DTRFA granted seven ad hoc post-retirement adjustments (in 1966, 1968, 1969, 1971, 1975, 1976, and 1981). These adjustments ranged from 3% to 10%, and averaged 7.0%.

2) Thirteenth Check. In 1985 (Laws 1985, Ch. 259) the prior approach of occasional ad hoc percentage increases ended, replaced by a 13th check post-retirement adjustment mechanism. The DTRFA board could provide a 13th check distribution if investment income was equal to at least 6% of the fund's asset value as of the end of the last fiscal year. The distribution could not exceed 1% of the fund's asset value. To allocate the available amount, the plan administration first added the years of service for all recipients plus the years in retirement status for all recipients. The result was the total units of the covered retirees and other benefit recipients. Dividing the total available excess assets by the total units resulted in the unit value. The unit values over time were:

Year	Unit Value	Year	Unit Value	Year	Unit Value
1985	$34	1989	$46	1993	$55
1986	$44	1990	$50	1994	$52
1987	$48	1991	$52	1995	$55
1988	--	1992	$50		

The amount any individual would receive was determined by multiplying the unit value for the given year by that person's years of service plus years in retirement. For example, in 1985, a DTRFA retiree retired for 10 years who had 30 years of service would have received a 13th check of $1,360, which equals $34 x 40. In 1990 (Laws 1990, Ch. 570, Art. 7, Sec. 4), DTRFA and SPTRFA were permitted to allow benefit recipients to annuitize the 13th check amount rather than receive the payment in a lump sum. The annuitized amount was based on the age of the annuitant or survivor, the plan's mortality table, and the interest rate assumption governing the Minnesota Post Retirement Investment Fund (Post Fund).

3) Automatic Percentage Increases plus Increases Based on Rate of Return in Excess of Assumption. In 1995 (Laws 1995, Ch. 262, Art. 2) the DTRFA 13th check provision was replaced by the same system which had been passed a few years earlier for the Minneapolis Teachers Retirement Fund Association (MTRFA), an association which has since consolidated into TRA. Under this approach, annuity payments were increased by 2% annually plus benefit recipients could receive an additional investment-related post-retirement adjustment based on the five-year annualized return above 8.5%, if any, with a minor adjustment for the contribution deficiency.

4) 2010 Financial Sustainability Provisions and Related Revisions. In 2010, as part of the Financial Sustainability legislation addressing the weak condition of Minnesota public pension plans following the collapse of the markets in 2008, the DTRFA post-retirement adjustment procedures were again revised (Laws 2010, Ch. 359, Art. 1, Sec. 60-62). The new procedure consisted of a transitional system followed by a move to an inflation match not to exceed 5%,

after funding ratios improved considerably. Under the transition method, DTRFA would provide no increase if the funding ratio based on market value (market value of assets divided by accrued liability) was less than 80%. A 1% increase would be paid if the funding ratio was at least 80% but less than 90%, and a 2% increase was to be paid if the ratio is at least 90%. When the funding ratio was at least 90%, the transition method ended and a new system put in place to match inflation up to 5%. However, no DTRFA post-retirement increase was every paid under the 2010 provisions, because in following years the funding ratio remained well under 80%. In 2013 (Laws 2013, Ch. 111, Art. 13, Sec. 10-11, 24) the approach created in 2010 was revised to pay a 1% increase to benefit recipients regardless of the funding ratio. Upon achieving a funding ratio of 90% or more, the 1% increase provision expires and an inflation match, not to exceed 5%, will be paid.

b. SPTRFA Adjustments.

1) Ad Hoc Increases. Before 1979, any SPTRFA post-retirement adjustments were on an ad hoc basis.

2) Thirteenth Check. The SPTRFA shifted to a 13th check approach in 1979, several years before the DTRFA. The SPTRFA special law authorized using 0.5% of the fund's asset value at the end of the prior fiscal year for the adjustment, if the SPTRFA investment income during the preceding fiscal year was in excess of 5.5% of the plan's asset value. To be eligible to share in the distribution, the annuitant had to be receiving an annuity for at least three years. The available amount was allocated based on each eligible recipient's credited years of service relative to the total years of service credit of all eligible recipients. With this allocation approach, the more service credit the teacher had at the time of retirement, the larger the 13th check that person would receive. The amount of the person's monthly benefit and the length of time in retirement did not factor at all into the calculation. In 1985, under Laws 1985, Ch. 259, the same legislation which created the DTRFA 13th check, the SPTRFA 13th check mechanism was significantly revised and made identical to the newly enacted DTRFA 13th check procedure. Thus, the allocation of the adjustment was based on units that combined both years of service credit and years of annuity receipt. In 1990 (Laws 1990, Ch. 570, Art. 7, Sec. 4), the DTRFA and SPTRFA were permitted to allow benefit recipients to annuitize the 13th check amount rather than receive the payment in a lump sum. The annuitized amount was based on the age of the annuitant or survivor, the plan's mortality table, and the interest rate assumption governing the Minnesota Post-Retirement Investment Fund (Post Fund).

3) Automatic Percentage Increases plus Increases Based on Rate of Return in Excess of Assumption. In 1997 (Laws 1997, Ch. 233, Art. 3, Sec. 7), the prior SPTRFA 13th check post-retirement adjustment mechanism was eliminated and was replaced with the same system that had been in place for the MTRFA for several years, and which had been authorized for the DTRFA in 1995. As described previously, the new system provided an automatic 2% annual increase plus a possible additional increase based on the five-year annualized return above 8.5%, if any, with a minor adjustment for the contribution deficiency. In 2006 (Laws 2006, Ch. 277, Art. 1, Sec. 2) a 5% cap was placed on SPTRFA post-retirement increases, although the cap was not to become effective until 2010.

4) Inflation Match. In 2007 (Laws 2007, Ch. 134, Art. 7, Sec. 1-2) under a temporary provision to be applicable for two years, the SPTRFA would provide post-retirement increases matching inflation up to 2.5%, or up to 5.0% if both the annual and the five-year average investment returns are at least 8.5%. In 2009 (Laws 2009, Ch. 169, Art. 7), notwithstanding prior law, the SPTRFA post-retirement mechanism was temporarily revised to provide post-retirement adjustments matching inflation up to 5%, without the need to meet any investment performance requirements. The revision was supposed to expire in 2011.

5) 2010 Financial Sustainability Provisions and Related Revisions. Due to 2010 legislation (Laws 2010, Ch. 359, Art. 1, Sec. 88), part of the Financial Sustainability Provisions, SPTRFA was prohibited from providing any post-retirement adjustment in 2011. In 2011 (1st Spec. Sess. Laws 2011, Ch. 8, Art. 2, Sec. 3-5, 22), the SPTRFA post-retirement adjustment authority was again revised. Under a transitional method beginning with the 2012 adjustment, SPTRFA would provide a 1% increase until the SPTRFA funding ratio is at least 80%, and a 2% increase when the funding ratio is at least 80% but less than 90%. When a 90% ratio is achieved, the transitional method expires and the SPTRFA will provide post-retirement adjustments matching inflation up to 5%.

c. MSRS, PERA, TRA Adjustments.

1) Ad Hoc Increases. MSRS, PERA, and TRA plans provided a few ad hoc post-retirement adjustments during the 1953-1969 period, with MSRS and PERA benefit recipients receiving three post-retirement adjustments. TRA benefit recipients received seven post-retirement adjustments, but four of these were directed to TRA retirees who were members of a prior TRA plan, to adjust their benefits to levels deemed more reasonable.

2) Automatic Post-Retirement Adjustments: Minnesota Adjustable Fixed Benefit Fund (MAFB). During the 1950s and much of the 1960s, considerable progress was made in increasing assets in Minnesota state public pension funds. When the pension funds amassed assets greater than the required reserves for retirees, this made it possible to consider a limited goal of providing periodic increases to retirees to help meet the increased cost of living. To do this without "raiding" the pension funds or the public treasury, the Legislature turned its attention to a mechanism providing increases funded from the yield or returns on investment assets in excess of the statutory assumptions.

The Minnesota Adjustable Fixed Benefit Fund (MAFB), created in 1969 (Laws 1969, Ch. 485, Sec. 32, and Ch. 914, Sec. 10), was the initial automatic post-retirement adjustment mechanism. Functionally, the MAFB was a variable annuity mechanism with an original benefit amount benefit floor. MAFB adjustments were to be wholly funded from investment gains in excess of the post-retirement interest rate actuarial assumption on the fully funded reserves for the retirement annuities covered by the mechanism. As originally enacted, if investment losses occurred previous post-retirement increases could be rolled back, but the retirement annuity amount originally payable at retirement was guaranteed.

To create the MAFB, the MSRS, PERA, and TRA plans transferred sufficient reserves to the MAFB to permit level annuities to be paid to retirees, providing the fund continued to earn at least the actuarial interest requirement. Annuity amounts were to be modified through an adjustment mechanism relying on a two-year average total rate of return measure, with the averaging intended to add some stability. The total rate of return included dividends, interest, and realized and unrealized gains or losses. Annually, a "benefit adjustment factor" was computed. This was calculated by dividing the result of one plus a two-year average total rate of return by one plus the actuarial return. If the fund was not meeting the actuarial investment earnings requirement, the ratio was less than one. If the return equaled the actuarial return, the ratio was equal to one. If the returns exceeded the actuarial return, the ratio would be greater than one. The MAFB law provided that benefits could be increased if the benefit adjustment factor was greater than 1.02, providing that certain additional requirements were met. If the benefit adjustment factor was less than 0.98, a benefit decrease was required, but at no time could the retirement benefits drop below the benefit level received on the date of retirement.

The benefit increases actually granted through the Minnesota Adjustable Fixed Benefit Fund (MAFB) were minimal. The MAFB only paid one set of increases operating as designed, in 1972 (MSRS-General: 2.0%; PERA-General: 4.0%; and TRA: 2.5%) differing among plans because mortality gains and losses were not isolated out of the formula until 1973. The unsatisfactory performance of the MAFB was due to an initial failure to isolate out mortality gains and losses in the first version of the adjustment formula, to the poor investment climate during the early 1970s, and to an annuity stabilization reserve requirement that was part of the MAFB adjustment process. Benefit increases above 4% could not be paid unless the annuity stabilization reserve contained enough assets to cover 15% of the past year's benefit payments. If the reserve was insufficient, part of the new investment earnings were added to the reserve rather than paid out as benefits. Benefit increases above 4% required correspondingly higher annuity reserves in the MAFB.

Through the remainder of the 1970s, the MAFB played no direct role in revising retiree benefit amounts. In 1973 (Laws 1973, Ch. 653, Sec. 28, 29, and Chapter 753, Sec. 39-41, 71) the Legislature passed a major restructuring of the way benefits in our plans are computed at the time of retirement. The 1973 legislation increased the interest rate actuarial assumption from 3.5% to 5.0%, but more importantly, it replaced the career average salary base with the highest five years average salary base for benefit calculations. This led to much higher benefits at the time of retirement. To address the much lower benefits being paid to pre-1973 retirees, the Legislature granted a two-part 25% post-retirement increase. The Legislature intervened again in 1978, allowing a 4.0% adjustment and overriding the MAFB formula, which would not have permitted payment of an increase.

3) Post Fund, 1980-1992. The Minnesota Adjustable Fixed Benefit Fund (MAFB) was substantially revised in 1980 (Laws 1980, Ch. 607, Art. 15, Sec. 16) and renamed the Minnesota Post Retirement Investment Fund (Post Fund). The 1980 Post Fund retained the MAFB's pooling of fully funded retirement annuity reserves, and increases were based on investment performance in excess of the post-retirement interest rate actuarial assumption akin to the MAFB, but the investment performance was determined on a yield basis (i.e., dividends on equities, interest on debt equities, and realized gains on the sale of investments) rather than the total rate of return used by the MAFB. A second difference was that the Post Fund contained no provisions for reducing benefit levels when investment returns were low. Third, the original Post Fund based adjustments on a single year's realized investment return, rather than using a multi-year period average.

   To compute benefit adjustments, at the end of each fiscal year (June 30) the required reserves were calculated. The required reserves were the assets needed to meet the current stream of annuity payments to be paid to retirees over time. The total reserves were multiplied by .05, the Post Fund interest assumption at that time, to determine the amount of investment income needed to sustain the current benefit level for the coming year. By subtracting this amount from actual total realized investment earnings, excess investment earnings were determined and were used to create a permanent increase in the annuities of retirees. The fiscal year information was used to determine the amount of increase, if any, payable on the next January 1, the effective date of any benefit increase. To determine benefit increases payable as of January 1, the excess investment income and the required reserves were projected forward to that date by increasing the excess investment income by 2.5%, the return which those funds must earn for the six month period in order to meet the actuarial assumption, and by estimating the total required reserves on January 1 for those eligible for a post-retirement adjustment.

   The 1980-1992 Post Fund paid increases in each of the 12 years that it was in effect. The average increase during the 12-year period was 6.5%.

4) Combined Cost-of-Living Component/Investment-Performance Component Post Fund. Significant changes in the Post Fund occurred in 1992 (Laws 1992, Ch. 530). The mechanism was revised to include two components rather than the prior single component. The combined components were:

   – Inflation Match Component. An annual post-retirement increase matching inflation, but not to exceed 3.5%, was created; and
   – Additional Asset Value-Based Component. An additional asset value-based increase was permitted if investment returns generated assets in excess of the asset values needed to fully fund the existing pensions plus cover the inflation match.

   The addition of an inflation match component to the Post Fund, measured by the annual increase in the Consumer Price Index (CPI), changed the effective post-retirement interest rate actuarial assumption from the previous understated 5% assumption to an 8.5% assumption (the official 5% rate plus 3.5% to account for the inflation component, equals 8.5%), if retiree reserves are fully funded. The additional asset value-based component of the adjustment was triggered by asset values, if any, in excess of full required reserves. If there was an excess, one-fifth of that excess was credited to the current year, one fifth credited to the second year, another fifth to the third year, a fifth to the fourth year, and a fifth to the fifth year. In a given year, if assets were less than the amounts needed to fully fund retiree benefits, then a negative amount was added to the five-year accounts. As this process operated over time, the accumulated amounts allocated to the current year (if the net total were positive) became the reserves used to fund further percentage increases in pensions, in addition to the inflation match.

   To understand how this system operated, let's assume that inflation is a consistent 3.5% per year. When individuals retire, reserves needed to fully fund their benefits were transferred to the Post Fund. These reserves would remain fully adequate if assets in the Post Fund earned a consistent 8.5% return. (This would keep the Post Fund funding ratio based on market (market value divided by liabilities) equal to 100%.) An 8.5% return would be sufficient to cover the 5% Post Fund interest assumption plus cover an annual 3.5% inflation adjustment. If returns exceeded 8.5%, this would permit payment of adjustments in addition to the inflation adjustment. If however, returns were less than 8.5%, particularly for several years, a few things would happen. The reserves needed to cover the pensions, which had been fully adequate when the individuals retired, would no longer be adequate. These reserves are invested, but the asset value of these reserves would be growing at less than 8.5% per year. If returns are negative, these assets would actually lose value. There would not be sufficient asset growth to cover the inflation adjustment, and negative values would be added to the five-year accounts. With several years of returns below the 8.5% assumption, possibly even negative returns, nothing beyond the inflation match would be paid. If, when the annual post-retirement adjustment calculation is made, this year's account has a negative balance, that negative balance is rolled forward to the next year. Thus, if there were prolonged period of returns below 8.5% there would be no adjustment beyond the mandatory inflation match, because there would be no reserves to finance further adjustments. There would be negative reserves, a hole that would need to be filled by a prolonged period of strong returns, or a few years of very high returns, before any adjustments beyond the inflation adjustment could be paid. Luckily, investment returns during the 1990s were strong. The 1992 revisions in the Post Fund resulted in the payment of post-retirement adjustments in each of the five years that this version of the mechanism was in effect. The average increase during the five-year period was 5.80%.

In 1997 (Laws 1997, Ch. 233, Art. 1, Sec. 5), the inflation match component was revised downward to 2.5% rather than 3.5%, and at the same time the Post Fund investment return assumption was revised from 5% to 6%, retaining the effective post-retirement interest rate actuarial assumption governing the mechanism at 8.5%. The revised Post Fund investment return assumption was part of a package of benefit changes intended to increase the benefit level payable at the time of retirement, at the expense of lower adjustments during retirement. The benefit accrual rates for all of the defined benefit plans participating in the Post Fund were increased. This change was in part financed by the revised Post Fund inflation-match component and investment component actuarial assumption. Fewer reserves are needed to support any given annuity if the assets are assumed to earn 6% prior to payout rather than 5%. The released reserves were used to cover higher benefits at the time of retirement. But the 1997 6% return requirement, rather than the prior 5%, leaves less of a margin between the Post Fund investment return assumption and the true long-term expected annual rate of return, which is 8.5%. The inflation match component was reduced from 3.5% to 2.5% to compensate. In effect, in 1997 a higher benefit at the time of retirement was traded for approximately 1.0% per year lower Post Fund inflation-related adjustments. The 1997 revisions in the Post Fund resulted in the payment of a post-retirement adjustment in each of the next nine years, generally in excess of the rate of inflation. The average increase during that period was 5.88%.

5) <u>Post Fund Dissolved</u>. During the late 1990s and early 2000s, the State Board of Investment and plan administrators became concerned that the Post Fund was generating increases in excess of inflation, sometimes considerably in excess, and that these increases would jeopardize plan financing if serious market downturns occurred (the annuity reserves would no longer be fully funded and the Post Fund funding ratio would be less than 100%).

   In 2006 (Laws 2006, Ch. 277, Art. 1, Sec. 1, 3) a 5% cap on Post Fund total annual increases was passed, but the cap was not to become effective until July1, 2010, to permit the applicable retirement plans to seek approval from the federal Internal Revenue Service for the change.

   The 2008 Legislature (Laws 2008, Ch. 349, Art. 1, Sec. 2-3) made this cap effective June 30, 2008. The 2008 Legislature also enacted more fundamental change (Laws 2008, Ch. 349, Art. 1, Sec. 1, and Article 2, Sec. 1-2). The funding ratio of the Post Fund was to be computed annually. If that funding ratio fell below 85% in two consecutive years or below 80% in one year, the Post Fund was to be dissolved. If that occurred, MSRS, PERA, and TRA benefit recipients would receive an annual 2.5% increase in lieu of any other adjustment. The June 30, 2008, actuarial work revealed that the Post Fund funding ratio was less than 80%, and the Post Fund was dissolved.

6) <u>2010 Financial Sustainability Provisions and Related Revisions</u>. The Great Recession which began in 2008 and the accompanying severe hit to pension fund asset value considerably harmed the pension funds. In 2010, the MSRS, PERA, and TRA plan administrators proposed a numerous revisions in plan benefits and funding to address the situation. The proposal was approved by the Commission and Legislature and was enacted as Laws 2010, Chapter 359, Article 1, Financial Sustainability Provisions, and included many revisions to post-retirement adjustment provisions.

3. 2010 Post-Retirement Adjustment Mechanism Financial Sustainability Provisions. The provisions in current law are largely as requested by plan administrators following the considerable loss in market value that occurred in 2008, during what has become called the "Great Recession." The provisions reflect MSRS, PERA, TRA, and first class city teacher plan proposals enacted as the Financial Sustainability Provisions (Laws 2010, Ch. 359, Art. 1). Some post-retirement provisions were further revised during 2011, 2012, and/or 2013.

   Leading into 2010, MSRS, PERA, and TRA post-retirement adjustment provisions were generally uniform. Plan law provided retirees with 2.5% annual post-retirement adjustments, with prorating for those retired less than one year. In 2010, these plan administrators proposed a considerable scaling back of adjustments until financial stability was regained. Lesser adjustments will be provided until financial stability is regained, with a return to "normal" adjustments when the plan is financially stable. While some adjustment may have been necessary to address the situation, the provisions reflect an abandonment of certain Commission principles. The currently permitted adjustments vary among plans, which is inconsistent with Principle II.C.6. , which can be interpreted as calling for comparable retirement benefits across comparable plans, and Principle II.C.8, which states that post-retirement adjustments ought to match inflation.

   In designing the provisions, the plan administrators chose to measure pension plan financial stability using a plan funding ratio, assets divided by accrued liabilities. A funding ratio measure is not ideal, although any measure has some drawback. The funding ratio is a snapshot of current condition, but says nothing about the adequacy of the underlying plan financing. A plan could have a funding ratio of 100% (its assets are equal to its accrued liabilities), but if the plan has a contribution deficiency (actual contributions less than the actuarially required contributions), the funding ratio will erode over time. On the other hand, a plan could have a low funding ratio, but if the contributions to the plan are equal to the actuarially determined required contributions, the plan's funding ratio will increase over time and the plan will become fully funded by the full funding date. If nothing else, a reasonably high funding ratio indicates that at least in the short term, the plan has sufficient assets to pay a post-retirement adjustment without noticeably depleting the asset base. In any event, the system in place for each plan uses a funding ratio or ratios.

   Reviewing the first row in the table indicates that while all plans use a target funding ratio or ratios to define funding stability, different plans use different ratios and in different ways. MSRS, PERA, and TRA plans all use a funding ratio or ratios based on market value rather than actuarial value. In a rising market the actuarial value will lag behind the current market value. Thus, using a funding ratio based on market value rather than actuarial value may allow the plan to hit the necessary funding ratio target sooner.

   The MSRS-General, MSRS-Correctional, Elected State Officers, and Legislators plans measure financial stability using a 90% funding ratio based on market, and they use it as a trigger. When the plan achieves a 90% funding ratio based on market, the provision specifying reduced adjustments expires and full adjustments are to be paid thereafter. The Judges Plan is similar, but two triggers are used. An adjustment of 1.5% will be made until the plan's market value funding ratio hits 70%. The provision providing that adjustment then expires and a 2% adjustment is permitted (the same rate as the reduced adjustments being paid by MSRS-General). When the Judges Plan is 90% funded, the 2% adjustment will expire and 2.5% adjustments will occur thereafter. MSRS-State Patrol also uses two triggers, but they are 85% and 90%, rather than the 70% and 90% used by the Judges Plan.

   PERA plans use a 90% ratio, like MSRS-General, but PERA uses it in a different way. Rather than being used as a trigger, the PERA 90% ratio is a permanent requirement. Reduced adjustments are made until the applicable plan is at least 90% funded, and PERA adds a requirement that this must occur in two consecutive valuations. Furthermore, if the funding ratio falls below 85% in two consecutive valuations or below 80% in one, reduced adjustments again apply.

   TRA uses the same approach as MSRS-General, a single 90% ratio used as a trigger rather than as a permanent requirement.

   The SPTRFA and DTRFA differ from each other and from all the other plans. The SPTRFA has two standards rather than triggers, but these expire when a final target ratio is first attained. Specifically, the SPTRA uses funding ratios based on actuarial value rather than market value. If that ratio is less than 80% in a given year a 1% adjustment will be paid. If in a given year the ratio is at least 80% but less than 90%, a 2% adjustment will be paid. So if the SPTRFA had an 85% ratio in a given year, it would provide a 2% increase, and if the next year the ratio was 78%, it would revert back to a 1% increase. But once the plan's ratio met or exceeded 90%, the 1% and 2% adjustment provisions would expire, and for this plan an inflation match not to exceed 5% would apply thereafter. In contrast, the DTRFA uses a single trigger followed by a blink-off inflation match. DTRFA currently provides a 1% adjustment. When the plan achieves a funding ratio based on actuarial value of at least 90%, the 1% adjustment provision expires and the plan will begin paying an inflation match not to exceed 5%. However, after the inflation match provision becomes effective, if the funding ratio based on actuarial value drops below 80% in a given year, no adjustment will be paid in that year.

The table also provides information on the level of adjustments when the plans have not attained or are not in a "funding stability" situation, for those individuals who are new to retirement and for those retired longer. Again, consistency across plans is lacking. The minimum period that a person has to be in benefit receipt status to qualify for an adjustment that is not prorated varies from 12 months (SPTRFA, DTRFA, and PERA plans including PERA-P&F benefit recipients who retired before June 2, 2014) to as long as 36 months (three years) for PERA-P&F retirees who retire after June 1, 2014. MSRS plans and TRA require an 18 month period in retirement for a non-prorated adjustment.

The minimum period that a person must be retired to receive a prorated adjustment varies from one month (PERA-General and PERA-Correctional) to 25 months in PERA-P&F for those retiring after June 1, 2014. DTRFA does not provide any prorated benefit. DTRFA retirees retired at least one year get a full 1% adjustment, while those retired less than one year receive nothing.

Those who qualify for the full adjustment when the plan is not in funding stability status receive between 1% and 2%, depending upon the plan and the situation. TRA will provide a 2% adjustment. Most MSRS plans will also provide a 2% adjustment, but the Judges plan will provide a 1.5% adjustment before the funding ratio is at least 70% and a 2% adjustment thereafter until the funding ratio hits 90%. The State Patrol Plan will pay 1% until an 85% ratio is achieved, and 1.5% thereafter until a 90% ratio is achieved. PERA plans and the DTRFA will pay 1%. The SPTRFA will pay 1% if the funding ratio is less than 80%, and 2% if the ratio is at least 80% but less than 90%.

Inconsistencies across plans will continue to exist when plans reach funding stability. The full adjustment will be a fixed 2.5% per year in MSRS plans, TRA, and PERA plans other than PERA-P&F. The PERA-P&F will provide an inflation match not to exceed 2.5%. The SPTRFA and DTRFA will provide an inflation match not to exceed 5%, but the DTRFA inflation match provision will blink-off whenever the plan's funding ratio based on actuarial value is less than 80%.

The minimum period in benefit receipt for a full adjustment when funding stability is achieved is 12 months in nearly all plans, but it will be 36 months (three years) in PERA-P&F. The minimum period in benefit receipt to qualify for a prorated adjustment will be one month in MSRS plans, TRA, and most PERA plans. PERA-P&F will require 25 months to qualify for a prorated adjustment. SPTRFA and DTRFA will require three months. The DTRFA will provide a prorated adjustment when funding stability is attained, but no prorated adjustments prior to funding stability. It is the only plan that has such an arrangement.

4. Discussion and Analysis of the Various Pre-2014 Post-retirement Adjustment Procedures. Principle II.C.8. of the Commission's Principles of Pension Policy states that post-retirement adjustments should be provided and ought to match inflation to retain retiree purchasing power. Despite that statement, Minnesota public pension plans have never had post-retirement adjustment procedures which are fully consistent with this statement. Every attempted approach has diverged from the standard.

   The initial post-retirement adjustments were ad hoc. These helped, but adjustments were sporadic and were never specifically intended to match inflation.

   Thirteenth check procedures provided adjustments with no relation to inflation. Individuals with the same amount of service (or service plus years in retirement) received the same dollar amount as an adjustment, regardless of the amount of the person's benefit. The lowest paid retired teacher and the highest paid retired school administrator would receive the same dollar adjustment if they had the same years of service. Also, these adjustments were not built into the base.

   The Post Fund, in its various formulations prior to being dissolved, provided a fixed annual percentage adjustment plus a possible additional adjustment based excess reserves, if any. The adjustments this system provided depended on investment market returns, because investment returns would determine whether there was asset value in the Post Fund in excess of necessary reserves to cover the existing pensions. The annual benefit adjustments this system provided did not track inflation because investment returns over time are not well correlated with inflation. Periods of high returns might occur in low inflation periods, while returns might be modest in high inflation periods. Depending on the returns generated in the investment market after given cohorts of individuals retired, some received adjustments in excess of inflation, sometimes greatly in excess, while others lost purchasing power.

After the Post Fund had been in operation in one form or another for many years, a system was put in place for the Minneapolis Teachers Retirement Fund Association (MTRFA) that had a superficial resemblance to the Post Fund. The MTRFA would provide an automatic 2.0% annual increase plus an additional investment performance based increase equal to the plan's five year annualized investment return above 8.5%. Thus if the annualized return was 12.5%, the excess return is 4% (12.5%-8.5% = 4%). This procedure was passed into law at the urging of the MTRFA. For years retirees from all the first class teacher plans were complaining to the administrators of their pension plan, and to legislators, that first class city retired teachers were receiving post-retirement adjustments inferior to those TRA retirees were receiving from the Post Fund. In response the MTRFA tried to come up with a procedure which it hoped would operate similar to the Post Fund and provide comparable adjustments. The best way to ensure comparable treatment would have been to create a mini-Post Fund for the MTRFA. The MTRFA rejected this idea, probably because it would have quickly led to an argument to merge the MTRFA into TRA. The MTRFA coordinated program was very similar to TRA's, and if MTRFAA retirees were to be treated identically to those of TRA, the best thing to do would have been to simply merge the MTRFA into TRA. The MTRFA also may not have had sufficient assets to create a mini-Post Fund. In any event, the MTRFA remained separate and the MTRFA procedure was enacted. A few years later, the MTRFA procedure was duplicated for use in the SPTRFA and DTRFA.

Despite the superficial similarities between the Post Fund and the first class city teacher plan procedure, there was a very important difference. Any increase for Post Fund retirees, beyond the automatic portion, had to be supported by assets. If the Post Fund lacked the assets to provide increases, no increase beyond the automatic portion was provided. In contrast, the first class city teacher plan procedure ignored the asset base. It did not shout off if the asset base was depleted. Increases beyond the automatic portion were based on "excess" investment rates of return. If the MTRFA, for example, had only $1,000 in assets, but had a 12.5% rate of return on those assets, the MTRFA procedure would indicate that a 6% increase should be paid to retirees (the automatic 2% plus the 4% excess return). This would have been impossible to support given the limited assets.

The MTRFA procedure, later also put in law for the DTRFA and SPTRFA, created perverse results and perverse incentives when plan assets became depleted. Under that procedure, if the plan had reached a point where the total plan assets were equal to the necessary reserves for retirees, strong investment returns would no longer play any role in helping to finance the plan. Any returns in excess of the rate of return assumption (8.5% at that time), simply went to support the existing retirees and their benefits. Nothing was left to help grow assets for active members, because there were no active member assets. If plan assets dropped below the assets needed to fully fund retire benefits, which did happen in the MTRFA, the fund was on a course to quickly consume itself. Strong investment returns would not help, and might actually cause harm by further increasing retiree benefit levels.

The MTRFA procedure did major harm to that plan. The MTRFA was eventually merged into TRA. The adoption by DTRFA and SPTRFA of that same procedure also harmed those pension funds. The DTRFA and SPTRFA remain freestanding for now, but might be merged into TRA during the coming session.

The plans that had been part of the Post Fund, MSRS, PERA, and TRA, moved to flat 2.5% annual adjustments following the dissolution of that fund. MSRS, PERA, and TRA administrators contended that 2.5% was a good approximation of long term inflation levels. Perhaps it is a good estimate, but in any given year inflation will vary. An approach that would be fully consistent with the Commission's policy document would be to simply provide an adjustment matching inflation.

The fixed 2.5% adjustments MSRS, PERA, and TRA plans were providing, and whatever adjustments the DTRFA and SPTRA provided at that time, were set aside in the wake of the Great Recession. Procedures put in place for all the plans in the Financial Sustainability Provisions of 2010 and later legislation stressed stemming the bleeding at the expense of adherence to Commission principles. Consistent treatment across plans and serious efforts to keep retirees whole were set aside until financial stability was regained. Any notion of a best policy to be followed by all plans was abandoned. Some of the differences may be due to necessity. But much of it stems from plan administrators, often bending to particular constituencies, playing the principle role in designing these procedures, rather than the Commission. The proposals, particularly those in 2010, were adopted without much Commission input or crafting; thus the results do not reflect the desire for consistency and fairness that had generally guided past Commissions.

While the provisions for each plan can be grouped into procedures followed before financial stability and those to be followed if and when financial stability is achieved, there is no consistency in how financial stability is measured, even among plans in the same system. All are based on a measured funding ratio or ratios, but some use ratios based on market value, some based on actuarial value, some use one ratio as a trigger, and some use two. Some use the ratio or ratios as permanent standards or requirements rather than one-time triggers. TRA and most MSRS plans use a single trigger, a 90% funding ratio based on market, but MSRS Judges uses two, a 70% and 90% ratio. MSRS State Patrol also uses two, but it uses 85% and 90%. PERA plans use a 90% ratio, but as an ongoing standard rather than a trigger. If the given PERA plan exceeds a 90% ratio (in two consecutive actuarial valuations), higher benefit adjustments can commence, but the earlier provisions do not expire. Lower adjustments are again applicable if the plan retreats below 90% funding. The SPTRFA and DTRFA use ratios based on actuarial value rather than market. SPTRFA uses two ratios, as ongoing standards; at least until a 90% ratio is achieved. Then an inflation match not to exceed 5% will be paid thereafter. The DTRFA uses one ratio, and uses it as a trigger.

The lower the adjustment provided by a plan and the longer that a retiree must wait to qualify for an adjustment, the more vulnerable that individual is to the eroding effect of inflation. While retirees from all the plans are impacted by the same inflation rate, the adjustments to offset some or all of the impact vary. Prior to achieving financial stability, some plans are providing 1% adjustments, others 2%, and a few are in between, with the Judges Plan and the State Patrol Plan paying 1.5%. Prior to financial stability, some of the plans provide a full adjustment after one year of retirement (12 months) while TRA and MSRS require a year and one-half (18 months). Certain PERA-P&F retirees will need to be retired three years before receiving their first full adjustment. This will make these retirees particularly vulnerable if inflation is high. Similarly, for very recent retirees, the minimum eligibility period for a prorated adjustment varies considerably. Prior to financial stability, the DTRFA will not provide any form of prorated adjustment. PERA plans will provide a prorated adjustment with as little as one month in retirement, except for post-June 1, 2014 PERA-P&F retirees, who must wait 25 months to qualify for a prorated benefit.

When financial stability status is reached, MSRS, TRA, and most PERA plans will pay a 2.5% increase, hopefully a reasonable approximation of inflation, but PERA-P&F will match inflation not to exceed 2.5%. Even if on average inflation is 2.5%, PERA-P&F retirees will lose purchasing power. These retirees will receive less than 2.5% in any year when inflation is less than 2.5%, and will never get more than 2.5% when inflation exceeds 2.5%. Thus, their average increase will be less than 2.5%. In contrast to all the other plans, the SPTRFA and DTRFA will match inflation not to exceed 5%. These two first class city teacher plans will be closer to the Commission's stated preferred post-retirement adjustment policy than any other plans.

Background Information on the Actuarial Value of Public Pension Plan Assets

Since the actuarial valuation procedure was initially codified for Minnesota defined benefit retirement plans in 1965, with the initial codification of public pension plan financial and actuarial reporting requirements, Minnesota public pension plans have utilized two different ways to establish the value of assets for determining the existence of and the size of unfunded actuarial accrued liabilities.

From 1965 to 1983, Minnesota Statutes, Sections 356.20 and 356.215, required that pension plan assets at book or cost value be used in making a comparison of plan assets with plan actuarial liabilities. Book value is the generally initial purchase price of the investment security or other marketable asset. For bonds (debt instruments), the investment value was at amortized cost. For stocks (equity investments), the investment value was at cost. For equipment, the investment was at cost less any accrued depreciation. For real estate, the statute was unclear.

In 1984, at the initiation of the Department of Finance, among various actuarial assumption and actuarial method changes, the actuarial value of assets determination procedure changed. The method defined the actuarial value of assets as the cost value of investments plus one-third of the difference between the cost value of investments and the market value of investments. The proposal for the actuarial value of assets determination procedure change was generated external to the Commission, and the rationale for the change is not well reflected in Commission office files for Laws 1984, Chapter 564. The change, however, clearly was an attempt to capture some of the stock and bond market appreciation that had occurred in the late 1970s and early 1980s and to have the actuarial value of assets more closely reflect market value than the prior book value definition of the actuarial value of assets.

In 2000 (Laws 2000, Ch. 461, Art. 1, Sec. 3), at the recommendation of the consulting actuarial firm retained by the Legislative Commission on Pensions and Retirement under Minnesota Statutes, Section 3.85, Milliman & Robertson, Inc., the actuarial value of assets determination procedure changed again. The actuarial value of assets, initially termed "current assets," is the market value of assets as of the end of the fiscal year reduced by a percentage of the difference between the actuarial net return on the market value of assets and the asset return expected during the fiscal year based on the interest rate assumption determined at the close of each of four preceding fiscal years. The percentage reduction was 20% for the least recent applicable year, 40% for the next least recent applicable year, 60% for the year two years previous, and 80% for the immediate prior year. The recommendation from the Commission's retained actuary, as represented by testimony from that actuary before the Commission, was intended to bring the value of assets closer to market value while using a smoothing device that would minimize or eliminate short-term market volatility.

In 2008 (Laws 2008, Ch. 349, Art. 10, Sec. 10), the term "current assets" was revised to "actuarial value of assets," with the reduction in the difference between the actual net market value change and the expected market value increase under the pre-retirement interest rate assumption for the year occurring four years prior to the valuation year increased from 10% to 20%.

The following compares the pre-1984 asset valuation determination procedure, the post-1984/pre-2000 asset valuation determination procedure, and the current asset valuation determination procedure for a representative statewide retirement plan, the Teachers Retirement Association (TRA), and a representative local retirement plan, the St. Paul Teachers Retirement Fund Association (SPTRFA), for the fiscal year ending on June 30, 2006, as examples:

Teachers Retirement Association (TRA)

	Pre-1984 Method	Post-1984/Pre-2000 Method	Current Method
Summary	Book or cost value of investment securities.	Cost value of investment securities plus one-third of the difference between the cost value and the market value of the investment securities.	Market Value, adjusted for amortization obligations receivable at the end of each fiscal year, less a percentage (20, 40, 60, or 80) of the Unrecognized Asset Return determined at the close of each of the four preceding fiscal years. Unrecognized Asset Return is the difference between actual net return on Market Value of Assets at the asset return expected during that fiscal year (based on the assumed interest rate employed in the July 1 Actuarial Valuation of the fiscal year).
Result	$19,649,139,143	$19,694,665,406	$19,035,611,839

Teachers Retirement Association (TRA)

	Pre-1984 Method		Post-1984/Pre-2000 Method		Current Method			
Calculation	Book Value	$19,649,139,143	Market Val.	$19,785,671,584	1. Market value of assets available for benefits			$19,785,671,584
			Book Value	$19,649,139,143			% Not	
			Difference	$136,532,441		Orig. Amt.	Recognized	
			Difference	$136,532,441	2. Calculation of unrecognized return			
			One-Third	x .3333	(a) Year ended 6/30/06	$653,165,303	80%	$522,532,242
			Market Adjust.	$45,506,263	(b) Year ended 6/30/05	$179,823,045	60%	$107,893,827
					(c) Year ended 6/30/04	$499,642,191	40%	$199,856,876
			Book Value	$19,649,159,143	(d) Year ended 6/30/03	($401,116,000)	20%	($80,223,200)
			Market Adjust	$45,506,263	(e) Year ended 6/30/02			$750,059,745
			Actuar. Val.	$19,694,665,406	3. Actuarial value of assets: ((1) - (2e)) ("Current Assets")			$19,035,611,839
Funding Impact	Act. Liab.	$20,679,110,879	Act. Liab.	$20,679,110,879	Act. Liab.	$20,679,110,879		
	Assets	$19,649,139,143	Assets	$19,694,658,742	Assets	$19,035,611,839		
	UAL	$1,029,971,736	UAL	$984,452,137	UAL	$1,643,499,040		
	Funding Ratio	95.02%	Funding Ratio	95.23%	Funding Ratio	92.05%		
	Normal Cost	$349,678,399	Normal Cost	$349,678,399	Normal Cost	$349,678,399		
	Expenses	$12,236,072	Expenses	$12,236,072	Expenses	$12,236,072		
	Amort.	$54,374,990	Amort.	$51,971,886	Amort.	$86,764,874		
	Act. Req.	$416,289,461	Act. Req.	$413,886,357	Act. Req.	$448,679,345		

St. Paul Teachers Retirement Fund Association (SPTRFA)

	Pre-1984 Method		Post-1984/Pre-2000 Method		Current Method			
Summary	Book or cost value of investment securities.		Cost value of investment securities plus one-third of the difference between the cost value and the market value of the investment securities.		Market Value, adjusted for amortization obligations receivable at the end of each fiscal year, less a percentage (20, 40, 60, or 80) of the Unrecognized Asset Return determined at the close of each of the four preceding fiscal years. Unrecognized Asset Return is the difference between actual net return on Market Value of Assets at the asset return expected during that fiscal year (based on the assumed interest rate employed in the July 1 Actuarial Valuation of the fiscal year).			
Result	$740,961,588		$829,213,976		$938,919,005			
Calculation	Book Value	$740,961,588	Market Val.	$1,005,745,229	1. Market value of assets available for benefits			$1,005,745,229
			Book Value	$740,961,588			% Not	
			Difference	$264,783,641		Orig. Amt.	Recognized	
					2. Calculation of unrecognized return			
			Difference	$264,783,641	(a) Year ended 6/30/06			$36,135,488
			One-Third	x .3333	(b) Year ended 6/30/05			$26,860,009
			Market Adjust.	$88,252,388	(c) Year ended 6/30/04			$82,512,072
					(d) Year ended 6/30/03			($56,015,000)
			Book Value	$740,961,588	(e) Year ended 6/30/02			
			Market Adjust	$88,252,388				
			Actuar. Val.	$829,213,976	3. Actuarial value of assets: ((1) - (2e)) ("Current Assets")			$938,919,005
Funding Impact	Act. Liab.	$1,358,619,906	Act. Liab.	$1,358,619,916	Act. Liab.	$1,358,619,906		
	Assets	$740,961,588	Assets	$829,252,388	Assets	$938,919,005		
	UAL	$617,658,318	UAL	$529,367,528	UAL	$419,700,901		
	Funding Ratio	54.54%	Funding Ratio	61.04%	Funding Ratio	69.11%		
	Normal Cost	$21,575,645	Normal Cost	$21,575,645	Normal Cost	$21,575,645		
	Expenses	$608,955	Expenses	$608,955	Expenses	$608,955		
	Amort.	$53,598,227	Amort.	$45,936,661	Amort.	$36,420,175		
	Act. Req.	$75,782,827	Act. Req.	$68,121,261	Act. Req.	$58,604,775		

Using an actuarial value of assets rather than the market value of assets for a pension plan apparently is not uncommon among public pension plans and complies with generally accepted accounting principles under Government Accounting Standards Board (GASB) pronouncements. Using a smoothing method that disregards short-term market volatility is particularly advantageous from a policy perspective if the pension plan funding procedures immediately translate actuarial results into modified employer contribution amounts in the following year, where short-term value changes would produce highly variable contribution levels year to year. In Minnesota, this was a consideration only for the Minneapolis Employees Retirement Fund (MERF) and for the five remaining local police and paid firefighter relief associations. The use of a smoothing mechanism may be sensible policy where the smoothing period reflects the actual pattern of market volatility, which tends to be either less than one year or longer than five years based on long-term stock market return data from Ibbotson Associates. Even if the smoothing period matches market cycles, an actuarial value of pension assets definition does nothing more than delay the recognition of actual market changes.

The following compares the actuarial value of assets and the market value of assets for the various statewide and major local retirement plans as of June 30, 2007, the high point in recent investment markets, as of June 30, 2010, after the recent investment market crash, and as of June 30, 2014, after the full impact of the 2008 market crash has worked through the formula::

June 30, 2007

Plan	Actuarial Value of Assets	Market Value of Assets	Actuarial Value as % of Market Value
MSRS-General	$8,904,516,772	$9,507,005,127	93.66%
MSRS-Correctional	$559,851,700	$595,057,508	94.08%
Judges	$153,561,828	$159,363,300	96.36%
State Patrol	$617,900,887	$649,181,278	95.18%
PERA-General	$12,985,324,048	$13,718,459,059	94.66%
PERA-Correctional	$5,198,921,940	$5,529,662,776	94.02%
PERA-P&F	$159,547,801	$174,280,940	91.55%
TRA	$1,383,741,762	$1,398,395,188	98.95%
DTRFA	$18,794,389,076	$19,938,881,872	94.26%
SPTRFA	$288,264,749	$318,973,530	90.37%
MERF	$1,015,722,034	$1,156,017,206	87.86%
Total	$50,061,742,597	$53,145,277,784	94.20%

June 30, 2010

Plan	Actuarial Value of Assets	Market Value of Assets	Actuarial Value as % of Market Value
MSRS-General	$8,960,391,000	$7,692,531,000	116.48%
MSRS-Correctional	$603,863,000	$525,245,000	114.97%
Judges	$144,728,000	$126,201,000	114.68%
State Patrol	$567,211,000	$488,870,000	116.02%
PERA-General	$13,126,993,000	$11,338,582,000	115.77%
PERA-Correctional	$5,188,339,000	$4,453,737,000	116.49%
PERA-P&F	$242,019,000	$211,368,000	114.50%
TRA			
DTRFA	$17,323,146,000	$14,917,240,000	116.13%
SPTRFA	$255,308,913	$192,402,546	132.70%
MERF	$1,001,444,000	$815,307,000	122.83%
Total	$47,413,442,913	$40,761,483,546	116.32%

June 30, 2014

Plan	Actuarial Value of Assets	Market Value of Assets	Actuarial Value as % of Market Value
MSRS-General	$10,326,272,000	$11,498,604,000	89.80%
MSRS-Correctional	$790,304,000	$877,056,000	90.11%
Judges	$157,52/8,000	$175,556,000	89.73%
State Patrol	$597,870,000	$667,340,000	89.59%
PERA-General	$15,326,272,000	$17,404,822,000	88.05%
PERA-Correctional	$4,100,489,000	$453,232,000	90.57%
PERA-P&F	$6,525,019,000	$7,273,100,000	89.71%
TRA	$18,181,932,000	$20,289,594,000	89.61%
DTRFA	$202,875,000	$226,071,000	89.74%
SPTRFA	$947,972,000	$1,045,400,000	90.68%
MERF Division	N/R	$935,946,000	--
Total	$45,882,429,000	$60,846,721,000	75.41%

The actuarial valuation of both pension liabilities and pension assets is problematic, at least from an accountant's point of view, because they are estimates of potential real life occurrences in advance of experiencing the occurrences.

In valuing pension liabilities, the time separation from the estimation of the magnitude of the liability and the actual discharge of the liability can be considerable and the only “real” or “accurate” determination of a pension plan’s ultimate pension liabilities occurs when all of the pension plan’s obligations have been paid and the pension plan is terminated.

In valuing pension assets, time is not the primary problem, but the primary problem is an assumption that the final market price of an investment sold by someone else on a given date by a market reporting mechanism could also be obtained by the pension plan if the plan sold all of its investments on that same date, even though an increase in the supply of investments for sale by that action should have a dampening effect on the available price. The problem of valuing pension plan assets is compounded by the considerable variability in market values from day to day, which makes the comparison of asset values on a predetermined date with the low variability of pension plan liabilities on a given date less reliable. In a recognition of the problematic nature of using a market value smoothing technique in determining the actuarial value of assets, as Minnesota Statutes, Section 356.215, does, a number of retirement plans utilize a “corridor” modification to the calculated actuarial valuation of assets, where the computed asset value is not permitted to exceed a percentage minimum or maximum of the market value of assets. The June 30, 2007, and June 30, 2010, comparative values above provide some sense of the potential differential between the two values without a “corridor” limitation.

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.... moves to amend H.F. No. 565; S.F. No. 519, as follows:

Page 2, line 1, strike "actuarial" and insert "market"

Page 2, line 20, delete"actuarial" and insert "market"

Page 3, line 18, delete"actuarial" and insert "market"

Page 3, after line 23, insert:

"Sec. 4. Minnesota Statutes 2014, section 356.20, subdivision 4, is amended to read:

Subd. 4. **Contents of financial report.** (a) The financial report required by this section must contain financial statements and disclosures that indicate the financial operations and position of the retirement plan and fund. The report must conform with generally accepted governmental accounting principles, applied on a consistent basis. The report must be audited.

(b) The report must include a statement that the actuarial valuation calculations prepared by the actuary retained under section 356.214 or by the actuary retained by the retirement fund or plan, whichever applies, comply with applicable actuarial requirements enumerated in section 356.215, and specified in the most recent standards for actuarial work adopted by the Legislative Commission on Pensions and Retirement. The ~~actuarial~~ market value of assets, the actuarial accrued liabilities, and the unfunded actuarial accrued liability of the fund or plan must be disclosed. The report must contain a certification by the actuary retained under section 356.214 or the actuary retained by the fund or plan, whichever applies, specifying that normal cost and the actuarial accrued liabilities for all benefits are computed in accordance with the entry age actuarial cost method and in accordance with the most recent applicable standards for actuarial work adopted by the Legislative Commission on Pensions and Retirement.

(c) The report must contain an itemized exhibit describing the administrative expenses of the plan, including, but not limited to, the following items, classified on a consistent basis from year to year, and with any further meaningful detail:

(1) personnel expenses;

(2) communication-related expenses;

(3) office building and maintenance expenses;

(4) professional services fees; and

(5) other expenses.

(d) The report must contain an itemized exhibit describing the investment expenses of the plan, including, but not limited to, the following items, classified on a consistent basis from year to year, and with any further meaningful detail:

(1) internal investment-related expenses; and

(2) external investment-related expenses.

(e) Any additional statements or exhibits or more detailed or subdivided itemization of a disclosure item that will enable the management of the plan to portray a true interpretation of the plan's financial condition must be included in the additional statements or exhibits.

EFFECTIVE DATE. This section is effective June 28, 2015, and applies to all actuarial reporting after that date.

Sec. 5. Minnesota Statutes 2014, section 356.215, subdivision 1, is amended to read:

Subdivision 1. **Definitions.** (a) For the purposes of sections 3.85 and 356.20 to 356.23, each of the terms in the following paragraphs has the meaning given.

(b) "Actuarial valuation" means a set of calculations prepared by an actuary retained under section 356.214 if so required under section 3.85, or otherwise, by an approved actuary, to determine the normal cost and the accrued actuarial liabilities of a benefit plan, according to the entry age actuarial cost method and based upon stated assumptions including, but not limited to rates of interest, mortality, salary increase, disability, withdrawal, and retirement and to determine the payment necessary to amortize over a stated period any unfunded accrued actuarial liability disclosed as a result of the actuarial valuation of the benefit plan.

(c) "Approved actuary" means a person who is regularly engaged in the business of providing actuarial services and who is a fellow in the Society of Actuaries.

(d) "Entry age actuarial cost method" means an actuarial cost method under which the actuarial present value of the projected benefits of each individual currently covered by the benefit plan and included in the actuarial valuation is allocated on a level basis over the service of the individual, if the benefit plan is governed by section 424A.093, or over the earnings of the individual, if the benefit plan is governed by any other law, between the entry age and the assumed exit age, with the portion of the actuarial present value which is allocated to the valuation year to be the normal cost and the portion of the actuarial present value not provided for at the valuation date by the actuarial present value of future normal costs to be the actuarial accrued liability, with aggregation in the calculation process to be the sum of the calculated result for each covered individual and with recognition given to any different benefit formulas which may apply to various periods of service.

(e) "Experience study" means a report providing experience data and an actuarial analysis of the adequacy of the actuarial assumptions on which actuarial valuations are based.

(f) "~~Actuarial~~ Value of assets" means the market value of all assets as of the preceding June 30~~, reduced by:~~.

~~(1) 20 percent of the difference between the actual net change in the market value of total assets between the June 30 that occurred three years earlier and the June 30 that occurred four years earlier and the computed increase in the market value of total assets over that fiscal year period if the assets had earned a rate of return on assets equal to the annual percentage preretirement interest rate assumption used in the actuarial valuation for the July 1 that occurred four years earlier;~~

~~(2) 40 percent of the difference between the actual net change in the market value of total assets between the June 30 that occurred two years earlier and the June 30 that occurred three years earlier and the computed increase in the market value of total assets over that fiscal year period if the assets had earned a rate of return on assets equal to the annual percentage preretirement interest rate assumption used in the actuarial valuation for the July 1 that occurred three years earlier;~~

~~(3) 60 percent of the difference between the actual net change in the market value of total assets between the June 30 that occurred one year earlier and the June 30 that occurred two years earlier and the computed increase in the market value of total assets over that fiscal year period if the assets had earned a rate of return on assets equal to the annual percentage preretirement interest rate assumption used in the actuarial valuation for the July 1 that occurred two years earlier; and~~

~~(4) 80 percent of the difference between the actual net change in the market value of total assets between the most recent June 30 and the June 30 that occurred one year earlier and the computed increase in the market value of total assets over that fiscal year period if the assets had earned a rate of return on assets equal to the annual percentage preretirement interest rate assumption used in the actuarial valuation for the July 1 that occurred one year earlier.~~

(g) "Unfunded actuarial accrued liability" means the total current and expected future benefit obligations, reduced by the sum of the ~~actuarial~~ value of assets and the present value of future normal costs.

(h) "Pension benefit obligation" means the actuarial present value of credited projected benefits, determined as the actuarial present value of benefits estimated to be payable in the future as a result of employee service attributing an equal benefit amount, including the effect of projected salary increases and any step rate benefit accrual rate differences, to each year of credited and expected future employee service.

EFFECTIVE DATE. This section is effective June 28, 2015, and applies to all actuarial reporting after that date."

Renumber the sections in sequence and correct the internal references

Amend the title accordingly

State of Minnesota

HOUSE OF REPRESENTATIVES

EIGHTY-NINTH SESSION

H. F. No. 565

02/05/2015 Authored by O'Driscoll
The bill was read for the first time and referred to the Committee on Government Operations and Elections Policy

A bill for an act

relating to retirement; general state employees retirement plan; correctional state employees retirement plan; State Patrol retirement plan; public employees police and fire retirement plan; Teachers Retirement Association; St. Paul Teachers Retirement Fund Association; modifying the financial sustainability triggers for postretirement adjustment mechanisms; amending Minnesota Statutes 2014, sections 354A.29, subdivisions 7, 8, 9; 356.415, subdivisions 1, 1a, 1c, 1d, 1e, 1f.

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

Section 1. Minnesota Statutes 2014, section 354A.29, subdivision 7, is amended to read:

Subd. 7. **Eligibility for payment of postretirement adjustments.** (a) Annually, after June 30, the board of trustees of the St. Paul Teachers Retirement Fund Association must determine the amount of any postretirement adjustment using the procedures in this subdivision and subdivision 8 or 9, whichever is applicable.

(b) On January 1, each ~~eligible~~ person who has been receiving an annuity or benefit under the articles of incorporation, the bylaws, or this chapter ~~for at least three calendar months as of the end of the last day of the previous calendar year~~, whose effective date of benefit commencement occurred on or before July 1 of the calendar year immediately before the adjustment, is eligible to receive a postretirement increase as specified in subdivision 8 or 9.

EFFECTIVE DATE. This section is effective June 30, 2015.

Sec. 2. Minnesota Statutes 2014, section 354A.29, subdivision 8, is amended to read:

Subd. 8. **Calculation of postretirement adjustments; ~~transitional provision~~ percentage based.** (a) For purposes of computing postretirement adjustments for eligible benefit recipients of the St. Paul Teachers Retirement Fund Association, the accrued liability funding ratio based on the actuarial value of assets of the plan as determined by the two most recent actuarial valuations prepared under sections 356.214 and 356.215 determines the postretirement increase, as follows:

Funding ratio	Postretirement increase
Less than 80 percent	1 percent
At least 80 percent but less than 90 percent	2 percent

(b) The amount determined under paragraph (a) is the full postretirement increase to be applied as a permanent increase to the regular payment of each eligible member on January 1 of the next calendar year. For any eligible member whose effective date of benefit commencement occurred ~~during~~ after January 1 of the calendar year immediately before the postretirement increase is applied, the ~~full increase~~ amount determined under paragraph (a) must be ~~prorated on the basis of whole calendar quarters in benefit payment status in the calendar year prior to the January 1 on which the postretirement increase is applied, calculated to the third decimal place~~ reduced by 50 percent.

(c) If the accrued liability funding ratio based on the actuarial value of assets is at least 90 percent in two consecutive actuarial valuations, ~~this subdivision expires and~~ subsequent postretirement increases must be paid as specified in subdivision 9.

(d) If, following a postretirement increase under paragraph (a), the accrued liability funding ratio, based on the actuarial value of assets, falls below 80 percent for two consecutive actuarial valuations, the applicable postretirement increase must be reduced to one percent until January 1 of the calendar year next following the date on which the requirements for an increase under paragraph (a) are again satisfied.

EFFECTIVE DATE. This section is effective June 30, 2015.

Sec. 3. Minnesota Statutes 2014, section 354A.29, subdivision 9, is amended to read:

Subd. 9. **Calculation of postretirement adjustments; CPI based.** (a) This subdivision applies if the requirements of subdivision 8 ~~has expired~~, paragraph (c), have been satisfied.

(b) A percentage adjustment must be computed and paid under this subdivision to eligible persons under subdivision 7. This adjustment is determined by reference to the Consumer Price Index for urban wage earners and clerical workers all items index as reported by the Bureau of Labor Statistics within the United States Department of Labor each year as part of the determination of annual cost-of-living adjustments to recipients of federal old-age, survivors, and disability insurance. For calculations of postretirement adjustments under paragraph (c), the term "average third quarter Consumer Price Index value" means the sum of the monthly index values as initially reported by the Bureau of Labor Statistics for the months of July, August, and September, divided by three.

(c) Before January 1 of each year, the executive director must calculate the amount of the postretirement adjustment by dividing the most recent average third quarter index value by the same average third quarter index value from the previous year, subtract one from the resulting quotient, and express the result as a percentage amount, which must be rounded to the nearest one-tenth of one percent.

(d) The amount calculated under paragraph (c) is the full postretirement adjustment to be applied as a permanent increase to the regular payment of each eligible member on January 1 of the next calendar year. For any eligible member whose effective date of benefit commencement occurred ~~during~~ after January 1 of the calendar year immediately before the postretirement adjustment is applied, the ~~full increase~~ amount determined under paragraph (c) must be ~~prorated on the basis of whole calendar quarters in benefit payment status in the calendar year prior to the January 1 on which the postretirement adjustment is applied, calculated to the third decimal place~~ reduced by 50 percent.

(e) The adjustment calculated under paragraph (c) must not be less than zero nor greater than five percent.

(f) In the event the accrued liability funding ratio based on the actuarial value of assets falls below 90 percent for two consecutive actuarial valuations, the applicable postretirement increase must be determined under subdivision 8 until January 1 of the calendar year next following the date on which the requirements of subdivision 8, paragraph (c), are again satisfied.

EFFECTIVE DATE. This section is effective June 30, 2015.

Sec. 4. Minnesota Statutes 2014, section 356.415, subdivision 1, is amended to read:

Subdivision 1. **Annual postretirement adjustments; generally.** (a) Except as otherwise provided in subdivision 1a, 1b, 1c, 1d, 1e, or 1f, retirement annuity, disability benefit, or survivor benefit recipients of a covered retirement plan are entitled to a postretirement adjustment annually on January 1, as follows:

(1) a postretirement increase of 2.5 percent must be applied each year, effective January 1, to the monthly annuity or benefit of each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least 12 full months ~~prior to~~ before the January 1 increase; and

(2) for each annuitant or benefit recipient who has been receiving an annuity or a benefit amount for at least one full month, but less than 12 full months as of the current June 30, an annual postretirement increase of 1/12 of 2.5 percent for each month that the

person has been receiving an annuity or benefit must be applied, effective on January 1 following the calendar year in which the person has been retired for less than 12 months.

(b) The increases provided by this subdivision commence on January 1, 2010.

(c) An increase in annuity or benefit payments under this section must be made automatically unless written notice is filed by the annuitant or benefit recipient with the executive director of the covered retirement plan requesting that the increase not be made.

EFFECTIVE DATE. This section is effective June 30, 2015.

Sec. 5. Minnesota Statutes 2014, section 356.415, subdivision 1a, is amended to read:

Subd. 1a. **Annual postretirement adjustments; Minnesota State Retirement System plans other than State Patrol retirement plan.** (a) Retirement annuity, disability benefit, or survivor benefit recipients of the legislators retirement plans, including constitutional officers as specified in chapter 3A, the general state employees retirement plan, the correctional state employees retirement plan, and the unclassified state employees retirement program~~, and the judges retirement plan~~ are entitled to a postretirement adjustment annually on January 1, as follows:

(1) for each successive January 1 if the definition of funding stability under paragraph (b) has not been met as of the prior July 1 for or with respect to the applicable retirement plan, a postretirement increase of two percent must be applied each year, effective on January 1, to the monthly annuity or benefit of each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least 18 full months before the January 1 increase; and

(2) for each successive January 1 if the definition of funding stability under paragraph (b) has not been met as of the prior July 1 for or with respect to the applicable retirement plan, for each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least ~~six~~ one full month, but less than 12 full months as of the current June 30, an annual postretirement increase of 1/12 of two percent for each month that the person has been receiving an annuity or benefit must be applied, effective January 1, following the calendar year in which the person has been retired for ~~at least six months, but has been retired for less than 18~~ 12 months.

(b) ~~The increases provided by this subdivision commence on January 1, 2011.~~ Increases under this subdivision for the general state employees retirement plan, or the correctional state employees retirement plan~~, or the judges retirement plan~~ terminate on December 31 of the calendar year in which two prior consecutive actuarial valuations prepared by the approved actuary under sections 356.214 and 356.215 and the standards for actuarial work promulgated by the Legislative Commission on Pensions and Retirement indicates that the market value of assets of the retirement plan equals or exceeds 90 percent of the actuarial accrued liability of the retirement plan and increases under subdivision 1 recommence after that date. Increases under this subdivision for the legislators retirement plan ~~or the elected state officers retirement plan~~, including the constitutional officers, and for the unclassified state employees retirement program terminate on December 31 of the calendar year in which ~~the~~ two prior consecutive actuarial ~~valuation~~ valuations prepared by the approved actuary under sections 356.214 and 356.215 and the standards for actuarial work promulgated by the Legislative Commission on Pensions and Retirement indicates that the market value of assets of the general state employees retirement plan equals or exceeds 90 percent of the actuarial accrued liability of the retirement plan and increases under subdivision 1 recommence after that date.

(c) After having met the definition of funding stability under paragraph (b), the increase provided in paragraph (a), clauses (1) and (2), rather than an increase under subdivision 1, for the general state employees retirement plan or the correctional state employees retirement plan, is again to be applied in a subsequent year or years if the market value of assets of the applicable plan equals or is less than:

(1) 85 percent of the actuarial accrued liabilities of the applicable plan for two consecutive actuarial valuations; or

(2) 80 percent of the actuarial accrued liabilities of the applicable plan for the most recent actuarial valuation.

After having met the definition of funding stability under paragraph (b), the increase provided in paragraph (a), clauses (1) and (2), rather than an increase under subdivision 1, for the legislators retirement plan, including the constitutional officers, and for the unclassified state employees retirement program, is again to be applied in a subsequent year or years if the market value of assets of the general state employees retirement plan equals or is less than:

(1) 85 percent of the actuarial accrued liabilities of the applicable plan for two consecutive actuarial valuations; or

(2) 80 percent of the actuarial accrued liabilities of the applicable plan for the most recent actuarial valuation.

~~(c)~~ (d) An increase in annuity or benefit payments under this subdivision must be made automatically unless written notice is filed by the annuitant or benefit recipient with the executive director of the applicable covered retirement plan requesting that the increase not be made.

EFFECTIVE DATE. This section is effective June 30, 2015.

Sec. 6. Minnesota Statutes 2014, section 356.415, subdivision 1c, is amended to read:

Subd. 1c. **Annual postretirement adjustments; PERA-police and fire.** (a) Retirement annuity, disability benefit, or survivor benefit recipients of the public employees police and fire retirement plan are entitled to a postretirement adjustment annually on January 1, ~~until~~ <u>if the definition of </u>funding stability ~~is restored~~<u> under paragraph (c) has not been met</u>, as follows:

(1) for each annuitant or benefit recipient whose annuity or benefit effective date is on or before June 1, 2014, who has been receiving the annuity or benefit for at least 12 full months as of the immediate preceding June 30, an amount equal to one percent in each year; or

(2) for each annuitant or benefit recipient whose annuity or benefit effective date is on or before June 1, 2014, who has been receiving the annuity or benefit for at least one full month, but not less than 11 months, as of the immediate preceding June 30, an amount equal to 1/12 of one percent for each month of annuity or benefit receipt; and

(3) for each annuitant or benefit recipient whose annuity or benefit effective date is after June 1, 2014, unless Laws 2014, chapter 296, article 13, section 27, applies, who will have been receiving an annuity or benefit for at least 36 full months as of the immediate preceding June 30, an amount equal to one percent; or

(4) for each annuitant or benefit recipient whose annuity or benefit effective date is after June 1, 2014, unless Laws 2014, chapter 296, article 13, section 27, applies, who has been receiving the annuity or benefit for at least 25 full months, but less than 36 months as of the immediate preceding June 30, an amount equal to 1/12 of one percent for each full month of annuity or benefit receipt during the fiscal year in which the annuity or benefit was effective.

(b) Retirement annuity, disability benefit, or survivor benefit recipients of the public employees police and fire retirement plan are entitled to a postretirement adjustment annually on each January 1 following the restoration of funding stability as defined under paragraph (c) and during the continuation of funding stability as defined under paragraph (c), as follows:

(1) for each annuitant or benefit recipient who has been receiving the annuity or benefit for at least 36 full months as of the immediate preceding June 30, an amount equal to ~~the percentage increase in the Consumer Price Index for urban wage earners and clerical workers all items index published by the Bureau of Labor Statistics of the United States Department of Labor between the immediate preceding June 30 and the June 30 occurring 12 months previous, but not to exceed~~ 2.5 percent; and

(2) for each annuitant or benefit recipient who has been receiving the annuity or benefit for at least 25 full months, but less than 36 full months, as of the immediate preceding June 30, an amount equal to 1/12 of ~~the percentage increase in the Consumer Price Index for urban wage earners and clerical workers all items index published by the Bureau of Labor Statistics of the United States Department of Labor between the immediate preceding June 30 and the June 30 occurring 12 months previous for each full month of annuity or benefit receipt during the fiscal year in which the annuity or benefit was effective, but not to exceed 1/12 of~~ 2.5 percent for each full month of annuity or benefit receipt during the fiscal year in which the annuity or benefit was effective.

(c) Funding stability is restored when the market value of assets of the public employees police and fire retirement plan equals or exceeds 90 percent of the actuarial accrued liabilities of the applicable plan in the two most recent consecutive actuarial valuations prepared under section 356.215 and under the standards for actuarial work of the Legislative Commission on Pensions and Retirement by the approved actuary retained by the Public Employees Retirement Association under section 356.214.

(d) After having met the definition of funding stability under paragraph (c), a full or prorated increase, as provided in paragraph (a), clause (1), (2), (3), or (4), whichever applies, rather than adjustments under paragraph (b), is again applied in a subsequent year or years if the market value of assets of the public employees police and fire retirement plan equals or is less than:

(1) 85 percent of the actuarial accrued liabilities of the applicable plan for two consecutive actuarial valuations; or

(2) 80 percent of the actuarial accrued liabilities of the applicable plan for the most recent actuarial valuation.

(e) An increase in annuity or benefit payments under this section must be made automatically unless written notice is filed by the annuitant or benefit recipient with the executive director of the Public Employees Retirement Association requesting that the increase not be made.

EFFECTIVE DATE. This section is effective June 30, 2015.

Sec. 7. Minnesota Statutes 2014, section 356.415, subdivision 1d, is amended to read:

Subd. 1d. **Teachers Retirement Association annual postretirement adjustments.** (a) Retirement annuity, disability benefit, or survivor benefit recipients of the Teachers Retirement Association are entitled to a postretirement adjustment annually on January 1, as follows:

(1) for ~~January 1, 2011, and January 1, 2012, no postretirement increase is payable;~~

~~(2) for January 1, 2013, and~~ each successive January 1 until funding stability is restored, a postretirement increase of two percent must be applied each year, effective on January 1, to the monthly annuity or benefit amount of each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least 18 full months prior to the January 1 increase;

~~(3)~~ (2) for ~~January 1, 2013, and~~ each successive January 1 until funding stability is restored, for each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least ~~six~~ one full month, but less than 12 full months ~~before the January 1 increase~~ as of the current June 30, an annual postretirement increase of 1/12 of two percent for each month the person has been receiving an annuity or benefit must be applied, effective the January 1~~, for which the person has been retired for at least six months but less than 18 months~~ following the calendar year in which the person retired;

~~(4)~~ (3) for each January 1 following the restoration of funding stability, a postretirement increase of 2.5 percent must be applied each year, effective January 1, to the monthly annuity or benefit amount of each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least 18 full months prior to the January 1 increase; and

~~(5)~~ (4) for each January 1 following the restoration of funding stability, for each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least ~~six~~ one month, but less than 12 full months ~~before the January 1 increase~~ as of the current June 30, an annual postretirement increase of 1/12 of 2.5 percent for each month the person has been receiving an annuity or benefit must be applied, effective the January 1~~, for which the person has been retired for at least six months but less than 18 months~~ following the calendar year in which the person retired.

(b) Funding stability is restored when the market value of assets of the Teachers Retirement Association equals or exceeds 90 percent of the actuarial accrued liabilities of the Teachers Retirement Association in the two most recent prior actuarial valuations prepared under section 356.215 and the standards for actuarial work by the approved actuary retained by the Teachers Retirement Association under section 356.214.

(c) After having met the definition of funding stability under paragraph (b), the increase provided in paragraph (a), clauses (1) and (2), rather than an increase under subdivision 1, or the increase under paragraph (a), clauses (3) and (4), is again to be applied in a subsequent year or years if the market value of assets of the plan equals or is less than:

(1) 85 percent of the actuarial accrued liabilities of the plan for two consecutive actuarial valuations; or

(2) 80 percent of the actuarial accrued liabilities of the plan for the most recent actuarial valuation.

~~(c)~~ (d) An increase in annuity or benefit payments under this section must be made automatically unless written notice is filed by the annuitant or benefit recipient with the executive director of the Teachers Retirement Association requesting that the increase not be made.

~~(d)~~ (e) The retirement annuity payable to a person who retires before becoming eligible for Social Security benefits and who has elected the optional payment as provided in section 354.35 must be treated as the sum of a period-certain retirement annuity and a life retirement annuity for the purposes of any postretirement adjustment. The period-certain retirement annuity plus the life retirement annuity must be the annuity amount payable until age 62, 65, or normal retirement age, as selected by the member at retirement, for an annuity amount payable under section 354.35. A postretirement adjustment granted on the period-certain retirement annuity must terminate when the period-certain retirement annuity terminates.

EFFECTIVE DATE. This section is effective June 30, 2015.

Sec. 8. Minnesota Statutes 2014, section 356.415, subdivision 1e, is amended to read:

Subd. 1e. **Annual postretirement adjustments; State Patrol retirement plan.** (a) Retirement annuity, disability benefit, or survivor benefit recipients of the State Patrol retirement plan are entitled to a postretirement adjustment annually on January 1 if the definition of funding stability under paragraph (b) has not been met, as follows:

(1) a postretirement increase of one percent must be applied each year, effective on January 1, to the monthly annuity or benefit of each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least 18 full months before the January 1 increase; and

(2) for each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least ~~six~~ one full month, but less than 12 full months as of the current June 30, an annual postretirement increase of 1/12 of one percent for each month that the person has been receiving an annuity or benefit must be applied, effective January 1, following the calendar year in which the person has been retired for ~~at least six months, but has been retired for~~ less than ~~18~~ 12 months.

(b) ~~The increases provided by this subdivision commence on January 1, 2014.~~ Increases under paragraph (a) for the State Patrol retirement plan terminate on December 31 of the calendar year in which two prior consecutive actuarial valuations for the plan prepared by the approved actuary under sections 356.214 and 356.215 and the standards for actuarial work promulgated by the Legislative Commission on Pensions and Retirement indicates that the market value of assets of the retirement plan equals or exceeds 85 percent of the actuarial accrued liability of the retirement plan; however, thereafter, increases under paragraph (a) become effective again on the December 31 of the calendar year in which the actuarial valuation, or prior consecutive actuarial valuations for the plan prepared by the approved actuary under sections 356.214 and 356.215 and the standards for actuarial work promulgated by the Legislative Commission on Pensions and Retirement indicates that the market value of the assets of the retirement plan equals or is less than 80 percent of the actuarial accrued liability of the retirement plan for two years, or equals or is less than 75 percent of the actuarial accrued liability of the retirement plan for one year and increases under paragraph (c) ~~recommence~~ commence after that date.

(c) Retirement annuity, disability benefit, or survivor benefit recipients of the State Patrol retirement plan are entitled to a postretirement adjustment annually on January 1, as follows:

(1) a postretirement increase of 1.5 percent must be applied each year, effective on January 1, to the monthly annuity or benefit of each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least 18 full months before the January 1 increase; and

(2) for each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least ~~six~~ one full month, but less than 12 full months as of the current June 30, an annual postretirement increase of 1/12 of 1.5 percent for each month that the person has been receiving an annuity or benefit must be applied, effective January 1, following the calendar year in which the person has been retired for ~~at least six months, but has been retired for~~ less than ~~18~~ 12 months.

(d) Increases under paragraph (c) for the State Patrol retirement plan terminate on December 31 of the calendar year in which two prior consecutive actuarial valuations prepared by the approved actuary under sections 356.214 and 356.215 and the standards for actuarial work adopted by the Legislative Commission on Pensions and Retirement indicates that the market value of assets of the retirement plan equals or exceeds 90 percent of the actuarial accrued liability of the retirement plan and increases under subdivision 1 recommence after that date.

(e) An increase in annuity or benefit payments under this subdivision must be made automatically unless written notice is filed by the annuitant or benefit recipient with the executive director of the applicable covered retirement plan requesting that the increase not be made.

EFFECTIVE DATE. This section is effective June 30, 2015.

Sec. 9. Minnesota Statutes 2014, section 356.415, subdivision 1f, is amended to read:

Subd. 1f. **Annual postretirement adjustments; Minnesota State Retirement System judges retirement plan.** (a) The increases provided under this subdivision begin on January 1, 2014, and are in lieu of increases under subdivision 1 or 1a for retirement annuity, disability benefit, or survivor benefit recipients of the judges retirement plan.

(b) Retirement annuity, disability benefit, or survivor benefit recipients of the judges retirement plan are entitled to a postretirement adjustment annually on January 1, as follows:

(1) a postretirement increase of 1.75 percent must be applied each year, effective on January 1, to the monthly annuity or benefit of each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least 18 full months before the January 1 increase; and

(2) for each annuitant or benefit recipient who has been receiving an annuity or a benefit for at least ~~six~~ one full month, but less than 12 full months as of the current June 30, an annual postretirement increase of 1/12 of 1.75 percent for each month that the person has been receiving an annuity or benefit must be applied, effective January 1, following the calendar year in which the person has been retired for ~~at least six months, but has been retired for~~ less than ~~18~~ 12 months.

(c) Increases under this subdivision terminate on December 31 of the calendar year in which two prior consecutive actuarial valuations prepared by the approved actuary under sections 356.214 and 356.215 and the standards for actuarial work promulgated by the Legislative Commission on Pensions and Retirement indicates that the market value of assets of the judges retirement plan equals or exceeds 70 percent of the actuarial accrued liability of the retirement plan. Increases under subdivision 1 or 1a, whichever is applicable, begin on the January 1 next following that date.

(d) An increase in annuity or benefit payments under this subdivision must be made automatically unless written notice is filed by the annuitant or benefit recipient with the executive director of the applicable covered retirement plan requesting that the increase not be made.

EFFECTIVE DATE. This section is effective June 30, 2015.