

Background Information on Legislator Pension Coverage

Before 1965

Before 1965, if a legislator wanted retirement coverage the only choice was coverage under the General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General). PERA-General was a basic plan, meaning that the employee did not have Social Security coverage for the public employment and no contributions were made into the federal Social Security program. (In contrast, a coordinated plan is a pension plan where the individual is also covered by Social Security for the employment.) PERA-General in 1965 used a career average salary and had back-loaded accrual rates, heavily favoring long-service employees. In a back-loaded plan the accrual rate used for early years of service is lower than the accrual rate used for later years. In PERA-General, the employee would eventually receive a benefit that was 1.0% of the career average salary for each of the first ten years of service, 2.0% for each year during the second decade of service, 2.5% for each year during the third decade, and 3.0% for each year thereafter.

The Legislators Retirement Plan

In 1965, when the Legislature created a separate Legislators Retirement Plan in the Minnesota State Retirement System (MSRS), current legislators and new members with prior PERA-General coverage had an option to retain PERA-General coverage. But all new legislators would be covered by the Legislators Retirement Plan. The motivation for establishing a separate Legislators Retirement Plan probably came from a growing recognition that the back-loaded PERA-General plan was not well suited to legislative retirement coverage, since the typical legislator would not be providing many decades of service. Another likely factor was the minimal salary paid to legislators. Since the pension benefit was based on salary, a higher accrual rate seemed necessary to generate a meaningful benefit.

The Legislators Retirement Plan that was created in 1965 used more generous accrual rates, and the rates were front-loaded rather than level or back-loaded. The Legislators Retirement Plan that was enacted was a basic plan providing a retirement benefit of 5% of the average monthly salary received during the final term of office for each of the first eight years of service, and an additional 2.5% per year for each year beyond eight. The plan also had a provision covering spouses of members who died in office, providing a benefit equal to half the retirement benefit, and an additional amount for dependent children.

The Legislators Retirement Plan was closed to new members in 1997. All legislators first elected after 1997 are covered by the Minnesota State Retirement System Unclassified Plan (MSRS-Unclassified), a defined contribution plan which is coordinated with Social Security. Existing legislators were given an option to elect Social Security coverage and MSRS-Unclassified for continuing coverage, rather than continuing in the Legislators Retirement Plan with no Social Security coverage.

The Legislators Retirement Plan has been revised numerous times since 1965:

- Several changes occurred in 1977 and 1978 (Laws 1977, Ch. 35, Sec. 12; Laws 1978, Ch. 796, Sec. 1-4). Beginning with the 1979 Legislative Session, the maximum benefit accrual rate for any new legislative service was set at 2.5%, rather than 5% for each of the first eight years and 2.5% per year thereafter. This accrual rate change was adopted in recognition of the changing nature of legislative work and increases in legislator salaries. Until the early 1970s, legislative salaries were minimal. In order to provide any meaningful retirement benefit, a very high benefit accrual rate was used for initial years of service. As legislative salaries increased in recognition that legislative work was becoming more like a full-time occupation, the Legislature recognized that it needed to revise the benefit accrual rates downward. Also, salary for pension purposes was redefined to exclude any additional compensation for leadership positions. A 20-year cap on creditable service was imposed. The plan was revised to use the high-five average salary rather than the average salary in the final term in office and the normal retirement age was increased from age 60 to age 62, with age 60 becoming the earliest age for retirement with a reduced annuity. Vesting for a retirement annuity was reduced from eight years to six years.
- In 1989 (Laws 1989, Ch. 319, Art. 16, Sec. 1-7), the definition of salary was changed to include regular and special session per diem payments, the deferred annuity augmentation rates were revised to 3% per year up to the year in which the former legislator becomes age 55 and 5% per year thereafter, the reduction factors for early retirement were revised to require a more substantial penalty, and the 20-year cap on service credit was removed. Members who were no longer

accruing service credit because their service exceeded 20 years were authorized to again begin accruing service credit.

- In 1992 (Laws 1992, Ch. 598, Art. 1, Sec. 1; Art. 4, Sec. 3, 5) the 1989 removal of the Legislators Retirement Plan service credit cap was made retroactive. Long-term legislators, including those in deferred status with uncredited service prior to June 2, 1989, due to the then-existing cap on service accrual, were authorized to purchase service credit for the uncredited period by paying 9% of salary received during the uncredited period plus 6% interest from the midpoint of the period of uncredited service to the date of payment. Payment had to be received prior to retirement or by January 1, 1994, whichever was earlier.
- In 1997 (Laws 1997, Ch. 233, Art. 2) the plan was closed to new legislators. New legislators are covered by the MSRS-Unclassified Program, and Legislators Retirement Plan members are permitted to transfer coverage to that defined contribution plan.
- In 2002 (Laws 2002, Ch. 392, Art. 15), legislators who had chosen to remain in the Legislators Retirement Plan were given an opportunity to elect Social Security coverage while remaining in the Legislators Retirement Plan, provided that they agreed to cover the Social Security employee and employer contribution requirement.
- In 2003 (1st Spec. Sess. Laws 2003, Ch. 1, Art. 2, Sec. 3, 136), the Legislators Retirement Plan was revised from a terminally funded plan, with transfer of full actuarial reserves to the Minnesota Post Retirement Investment Fund (Post Fund) to cover expected lifetime annuity payments, to a pay-as-you-go plan for new retirees. No assets were transferred to the Post Fund for new retirees; instead, annual appropriations are made from the state general fund as necessary to cover the annual benefits.
- In 2006 (Laws 2006, Ch. 271, Art. 10), the plan's surviving spouse benefit provision was revised to be consistent with other MSRS defined benefit plans, permitting the survivor spouse of a legislator who dies in office to start receiving a surviving spouse joint-and-survivor annuity as early as age 55 rather than at a minimum of age 60. The remainder of the Legislators Retirement Plan chapter was recodified to improve clarity.
- In 2009 (Laws 2009, Ch. 169, Art. 1, Sec. 1-5) the Minnesota Post Retirement Investment Fund was dissolved. Another fund was created to receive any assets from the Post Fund which were applicable to legislators who retired before 2003 and to surviving spouses. The post-retirement adjustment procedures of the Post Fund were stricken, and in its place a fixed 2.5% annual increase was to be paid.
- In 2010 (Laws 2010, Ch. 359, Art. 1, Sec. 1, 76, 77) the deferred annuity augmentation rate was revised downward to 2.0% per year beginning January 1, 2011. Also in 2010, the post-retirement adjustment provision which provided a 2.5% per-year increase was temporarily revised to provide a 2.0% annual increase until financial stability is achieved, defined as when the funding ratio of MSRS-General based on market value is at least 90%.
- In 2011 (1st Spec. Sess. Laws 2011, Ch. 10, Art. 1, Sec. 28), for the biennium, \$4.881 million was appropriated to pay legislative retirement allowance and survivor benefits. If that amount is insufficient, the fund created in 2009 to accept assets applicable to legislators from the Post Fund is to be tapped for needed amounts.

MSRS-Unclassified Coverage for Post-1997 Legislators and Constitutional Officers, and Existing Legislators and Constitutional Officers Electing That Coverage

Defined benefit plan coverage utilizes a formula to determine the retirement annuity, typically by using a percentage benefit accrual rate per year of service applied to a designated salary base. Defined contribution plan coverage, similar to a 401(k) plan or an Individual Retirement Account (IRA), amasses contributions and investment returns that either can be taken as a lump sum payment upon retirement or can be converted to a life annuity.

Prior to 1997, legislators were covered by the Legislators Retirement Plan, a basic defined benefit plan. However, benefit increase legislation assembled in 1997 by the Minnesota State Retirement System (MSRS), the Public Employees Retirement Association (PERA), and the Teachers Retirement Association (TRA) included provisions revising pension coverage for legislators and constitutional officers. Laws 1997, Chapter 233, Article 2, required all legislators first elected after June 30, 1997, to be covered by a defined contribution plan, the Unclassified State Employees Retirement Program of

the Minnesota State Retirement System (MSRS-Unclassified), which is a coordinated plan, rather than the Legislators Retirement Plan.

MSRS-Unclassified also provides coverage to certain legislators first elected before 1997, because the 1997 legislation included a Social Security referendum for pre-1997 legislators, giving them a chance to elect Social Security coverage. Any legislator electing to have Social Security coverage was placed in MSRS-Unclassified for continuing service.

The 1997 legislation also treated constitutional officers in a manner similar to legislators. Any newly elected constitutional officer after 1997 is covered by MSRS-Unclassified, rather than the basic defined benefit Elective State Officers Plan. Constitutional officers first elected prior to 1997 were permitted to elect Social Security coverage, and be covered by that system plus MSRS-Unclassified for continuing service.

The 1997 legislation included a required study by the Legislative Commission on Pensions and Retirement of the appropriateness of the legislator and constitutional officer coverage change. The Commission completed the mandated study during the 1997-1998 interim and concluded that the coverage change was appropriate and recommended retaining the 1997 provisions.

Post-1997 Continuing Defined Contribution/Defined Benefit Coverage Issue

An MSRS-Unclassified Program provision, Minnesota Statutes, Section 352D.02, Subdivision 1, permitted employees to choose between the MSRS-Unclassified Program and MSRS-General within the first year of employment, with the MSRS-Unclassified Program being the default if no coverage was specifically chosen. However, given the presumption in the 1997 legislation that defined benefit plan coverage was not appropriate for legislators, this subdivision was revised in that legislation to exclude legislators. They were to be limited to the MSRS-Unclassified Program. However, Subdivision 3 in that section appeared to permit employees with MSRS-Unclassified Program coverage to transfer to MSRS-General after the individual had provided at least ten years of service. While the application to legislators was unclear from the wording of that provision, MSRS administrators took the position that a legislator was not an employee for purposes of that transfer provision and that long-service legislators were not eligible to transfer coverage.

Some legislators later questioned the 1997 changes which placed legislators in the MSRS-Unclassified Program. In 2008, H.F. 3223 (Mahoney); S.F. 3054 (Tomassoni) proposed revising the MSRS-Unclassified first-year-of-coverage provision to permit legislators, judges, the governor, the lieutenant governor, the secretary of state, the state auditor, and the attorney general to choose between MSRS-Unclassified and MSRS-General during the first year. The bill also proposed revising the coverage transfer-after-ten-years provision to explicitly include legislators and other elected officials. However, the bill did not pass. H.F. 3223 (Mahoney); S.F. 3054 (Tomassoni) was initially made part of the 2008 Omnibus Retirement Bill but was removed on the Senate Floor, through an amendment authored by then Commission Chair, Senator Don Betzold, and the Senate position prevailed in the conference committee.

The 2010 Omnibus Retirement Bill, passed as Laws 2010, Chapter 359, included many provisions trimming pension plan benefits in order to address pension plan liabilities. The bill was in response to the market meltdown of 2008 and early 2009, which substantially lowered pension plan assets. Most of the provisions which trimmed liabilities and shored up pension assets were contained in Article 1, the Financial Sustainability Provisions. However, other provisions trimming liabilities were found elsewhere in the bill. Article 4 revised MSRS-Unclassified Program provisions. MSRS had long expressed concern that the MSRS-Unclassified ten-year-transfer provision imposed added liability on MSRS-General, because those transferring into MSRS-General added more liability to the plan than they added in assets. Among the revisions in Article 4 was a revision to the ten-year transfer provision limiting the right to transfer after ten or more years to those first employed before July 1, 2010. For those first employed on or after that date, if they are to transfer they must do so before accruing seven years service. The provision was also revised by adding language explicitly excluding legislators, judges, and other elected officials from any right to transfer to MSRS-General.

Thus, any legislator in the MSRS-Unclassified Program clearly is not permitted to transfer to another plan. The legislators covered by the MSRS-Unclassified Program are those first elected after June 30, 1997, and also any legislator first elected before that date who chose to transfer to the MSRS-Unclassified Program.

Legislators Retirement Plan: Creating a Coordinated Program

Laws 1997, Chapter 233, Article 2, gave each sitting legislator first elected before July 1997 an option. He or she could choose to be treated like a new legislator and have MSRS-Unclassified coverage for continuing legislative service with Social Security coordination, or he or she could remain in the Legislators Retirement Plan with no Social Security coverage.

Sitting legislators who in 1998 declined Social Security coverage presumably felt the added value of Social Security coverage was not sufficient to justify leaving the Legislators Retirement Plan for prospective service. Later, however, some legislators who remained in the Legislators Retirement Plan became convinced that they would be better off having Social Security coverage for their legislative service. This may have been due to the impact that provisions of Social Security law might have on the Social Security benefit to which they would be entitled due to non-legislative employment for which they had Social Security coverage, and by another provision of Social Security law, called the Government Pension Offset, which can significantly reduce the spousal or widow (widower) Social Security benefit which they might receive based on a spouse's Social Security coverage. A provision of federal law waived any reduction under the Government Pension Offset if the individual was contributing to Social Security immediately prior to leaving employment. For some individuals, this may have provided a considerable incentive to elect Social Security coverage for their legislative employment.

In 2001, S.F. 1863 (Rest); H.F. 1896 (Skoglund) was introduced on behalf of a small group of legislators who declined Social Security coverage under the 1998 coverage election, rather than obtaining that coverage and having prospective service covered by MSRS-Unclassified. Under S.F. 1863 (Rest); H.F. 1896 (Skoglund), those legislators who earlier had declined Social Security coverage would be permitted to have a second Social Security election. If that coverage were elected, the employee would begin paying into the Social Security system and would be permitted to remain in the Legislators Retirement Plan for continuing legislative service, in a new coordinated program. Previously, the Legislators Retirement Plan was strictly a basic plan. The benefits and contribution rates in that new coordinated program would be identical to the benefits and contribution rates found in the basic program of the Legislators Retirement Plan. This raised policy issues:

1. Consistency and Fairness. The bill treated comparable employees differently. Some legislators, those first elected after June 1997, have defined contribution plan coverage and Social Security coverage, some pre-1997 legislators also have that defined contribution plan coverage plus Social Security because of the coverage they selected in 1998, while other pre-1997 legislators would now be permitted to have Social Security coverage while remaining in the defined benefit Legislators Retirement Plan.
2. Proper Contribution Rates and Benefit Levels. Another issue was whether benefits and contribution rates in the proposed Legislators Retirement Plan coordinated program should be reduced below those of the basic program. 2001 S.F. 1863 (Rest); H.F. 1896 (Skoglund) did not include any reduction in the benefits or contribution rates under the Legislators Retirement Plan. In general, when a coordinated program is created, the benefits provided by that coordinated plan (and the related contribution requirements) are reduced in recognition that the individual can also expect to receive Social Security benefits due to the covered employment. For example, the accrual rate (percentage of the high-five average salary which the individual will receive per year of service) for retirement at normal retirement age is 2.7% in the PERA-General basic plan, while the comparable accrual rate in the PERA-General Coordinated Plan is 1.7%. Contribution rates are much lower in PERA-General's Coordinated Plan compared to the Basic Plan in recognition that a less costly benefit was being provided under the Coordinated Plan. However, when a coordinated program was established in the Judges Retirement Plan many years ago, the benefits and contribution rates for the coordinated program of the Judges Retirement Plan were made the same as in the basic Judges Retirement Plan.

The Commission did not recommend that S.F. 1863 (Rest); H.F. 1896 (Skoglund) should pass, and the bill was not enacted.

However, in 2002 comparable provisions were added to the 2002 Omnibus Pension Bill and were enacted as Laws 2002, Chapter 392, Article 15. These provisions were added by amendment late in the process. Perhaps in an effort to make the provisions more palatable and to avoid any fiscal impact on the employer, the language included a requirement that any employee who elected Social Security coverage under the second Social Security referendum had to pay both the Social Security employee contribution and the Social Security employer contribution.