Background Information on Minnesota Defined Benefit Retirement Plans and Defined Contribution Retirement Plans

1. General Distinction Between Plan Types

   There are two major factors or elements in designing retirement plans. These are the level of the benefits and the level of contributions. When one factor is fixed or made pre-determinable, the other factor is automatically made variable. If the level of benefits or computation of benefits is fixed or established by formula in law, the plan is a defined benefit plan, and the contribution rate is variable, adjusted as necessary to ensure that the liabilities of the plan are covered. If the level of contribution is fixed, the plan is a defined contribution plan. With a defined contribution plan, the benefit level is unspecified. The benefit level will ultimately be determined through the investment markets, which will determine the growth of the assets prior to distribution.

   a. Defined Contribution Plans. The Unclassified State Employees Retirement Program of the Minnesota State Retirement System (MSRS-Unclassified) is one of several defined contribution plans found in Minnesota public pension law. The plan provides coverage for legislative employees (unless General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General) coverage is elected instead), many legislators, various individuals in the Executive Branch in unclassified positions, and some higher education managerial employees. In a defined contribution retirement plan, the level of contributions or the amount of member and/or employer funding is specified or fixed in some manner, making the level of eventual benefits and/or their duration the variable factor. Most commonly, in a defined contribution plan, the funding of the plan is specified as a percentage of the covered payroll of plan members. Those contributions, allocated to individual accounts and frequently invested based on individual selection, along with any investment return obtained, constitute the benefit available to the plan member upon termination of employment or retirement. Most commonly, the individual account balance is payable in a lump sum upon the termination of plan coverage or is available to be transferred to an insurance company for the purchase of a retirement annuity. Some retirement plans that generally are classified as defined contribution plans permit the individual account balance amount to be converted into a retirement annuity within the retirement plan at a specified rate, although the assumption of that retirement annuity mortality risk actually defines the post-retirement benefit amount and subjects the retirement plan to potential future mortality and investment return experience losses and a chance for an unfunded actuarial accrued liability, akin to a defined benefit plan.

   b. Defined Benefit Plans. MSRS-General is a defined benefit retirement plan. In a defined benefit plan, the level of benefits at the time of retirement or after retirement is specified or fixed in some manner, making the level of contributions or the amount of funding from period to period the variable factor. Most commonly, in a defined benefit plan, the retirement benefit is specified as a percentage of the final salary or of the final average salary per year of credited service rendered. Thus, the plan tracks and awards allowable service credit and salary credit and amasses a liability for the service and salary credit rendered to date that requires the periodic calculation and assessment by an actuary. The resulting actuarial valuation report both assesses the amount of actuarial accrued liability that the retirement plan has amassed to date and the amount of total contributions needed for the future plan year or plan years. Most commonly, in defined benefit plans, any lump sum amount is limited to a pre-retirement employment termination member contribution refund, with the regular retirement benefit only payable as a retirement annuity. Generally, a regular retirement annuity has optional equivalent value forms that open for election by the plan member. Retirement plans that are defined benefit plans can take on defined contribution retirement plan aspects, such as determining postretirement adjustment amounts from the amount of investment gain in whole or in part generated by the plan.

      In an actuarial report, the actuary determines the cost of the defined benefit plan being studied. This cost, usually specified as a percentage of covered payroll, is certainly strongly influenced by the specific benefits offered by the plan. But the cost of any given set of benefit provisions is dependent on many factors, such as the investment earnings rate assumptions, the average age and the age distribution of the covered membership, expected salary growth over the employee's remaining employment prior to retirement, turnover (the probabilities that employees remain in covered employment to draw benefits), probabilities of disability, and mortality conditions before and after retirement.

In computing the plan costs, the actuary will divide the cost into three elements. The first element is the contribution amount necessary to cover the plan's ongoing expenses, for staff salary, equipment, lease space, and all the other expenses related to operating a pension organization. The second element is the normal cost. The normal cost is the level contribution as a percentage of salary which will fund the current retirement plan benefits if made from first employment until retirement. Under general Commission policy, the normal cost contribution plus the contribution for expenses is shared equally between the employees and employer in nonpublic safety plans, while in public safety plans these costs are split on a 40%/60% basis between employees and employers. Often, the accumulated contributions made to the plan are less than the current liabilities. This creates an additional cost element, an amortization contribution sufficient to pay off the uncovered liabilities by the plan's full funding date. An amortization requirement can arise from many sources. Turnover which is less than expected, an increase in life expectancy, or investment earnings below the assumed rate can create a computed amortization requirement. Another common source is benefit improvements. Whenever benefits in a plan are improved, the contributions made in the past to cover normal costs, which were based on the plan cost prior to the benefit improvement, are inadequate to cover the liabilities imposed by the new, revised benefit plan. When an unfunded liability occurs, this added amortization cost may be covered by an employer additional contribution requirement.

2. Defined Benefit Plans and Defined Contribution Plans in Minnesota. In Minnesota, public pension plans by both number and membership are predominantly defined benefit pension plans. The following is a list of defined benefit Minnesota public pension plans and defined contribution Minnesota public pension plans.

Defined Benefit Plans	Defined Contribution Plans
1. General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General)	1. Unclassified Employees Retirement Program of the Minnesota State Retirement System (MSRS-Unclassified)
2. Correctional Employees Retirement Plan of the Minnesota State Retirement System (MSRS-Correctional)	2. PERA Defined Contribution Retirement Plan
3. MSRS Military Affairs Retirement Plan	3. Individual Retirement Account Plan (IRAP)
4. MSRS Transportation Department Pilots Retirement	4. College and University Supplemental Retirement Plan
5. State Patrol Retirement Plan	5. Volunteer Firefighters Relief Associations (about 75)
6. MSRS Elective State Officers Retirement Plan	6. Ambulance Personnel Longevity Plan
7. MSRS Legislators Retirement Plan	7. Hennepin County Supplemental Retirement Plan
8. MSRS Judges Retirement Plan	8. University of Minnesota Faculty Plan
9. General Employees Retirement Plan of the Public Employees Retirement Association (PERA-General)	9. Public Employee Supplemental Thrift Plan through State Deferred Compensation Plan or selected tax-sheltered annuity programs
10. Public Employees Police and Fire Retirement Plan (PERA-P&F)	10. Housing and Redevelopment Agency Retirement Plans
11. Local Government Correctional Service Retirement Plan (PERA-Correctional)	11. Pre-1971 School District Supplemental Retirement Plans (total of 8)
12. Public Employees Retirement Association Statewide Lump-Sum Volunteer Firefighter Retirement Plan (PERA-SVFP)	
13. Teachers Retirement Association (TRA)	
14. Duluth Teachers Retirement Fund Association (DTRFA)	
15. St. Paul Teachers Retirement Fund Association (SPTRFA)	
16. Fairmont Police Relief Association	
17. Virginia Fire Relief Association	
18. Volunteer Firefighter Relief Associations (about 625)	
19. University of Minnesota Faculty Supplemental Plan	