

## Background Information on the Unclassified State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-Unclassified)

1. In General. The Unclassified State Employees Retirement Program of the Minnesota State Retirement System (MSRS-Unclassified) was established in 1971 (Laws 1971, Ch. 604), and is governed by Minnesota Statutes, Chapter 352D.
2. Establishment. MSRS-Unclassified is a defined contribution plan established by Minnesota Statutes, Chapter 352D. The retirement program was developed on behalf of the commissioners of the various departments in the Executive Branch in state government. It was premised on the unattractiveness in 1971 of the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General) for upper echelon officials in state government who were unlikely to spend enough time in state employment to meet the MSRS-General vesting provision of ten years of service then applicable in 1971. It was intended to be an attractive fringe benefit to aid in the recruitment of department heads in state government. Since 1971, there have been numerous expansions in program coverage and modifications in coverage after established, as summarized in Item 12.
3. Program Coverage. The program currently covers a number of state employees or officers in the unclassified service of the State of Minnesota on either a mandatory or on an optional basis. The individuals specified in (a), (e), and (g), if first elected after June 30, 1997, below are members of the program on a mandatory basis and the remaining individuals have the option to elect to be members of the program rather than being a member of MSRS-General. The program membership includes:
  - a. the Governor, Lieutenant Governor, Secretary of State, State Auditor, and Attorney General;
  - b. an employee in the office of the Governor, Lt. Governor, Secretary of State, State Auditor, or Attorney General;
  - c. an employee of the State Board of Investment;
  - d. the head of a department, a division, or an agency created by statute in the unclassified service;
  - e. a member of the legislature;
  - f. a permanent, full-time unclassified employee of the legislature or a commission or an agency of the legislature;
  - g. the regional administrator or executive director of the Metropolitan Council, its general counsel, division directors, operations managers, and other positions as designated by the council;
  - h. the executive director, associate executive director of the Higher Education Services Office in the unclassified service;
  - i. the clerk of the appellate court;
  - j. the chief executive officers of correctional facilities, hospitals, and nursing homes;
  - k. an employee of the state ceremonial house;
  - l. an employee of the Minnesota Educational Computing Corporation;
  - m. an employee of the World Trade Center board;
  - n. an employee of the State Lottery board; and
  - o. a judge whose service has exceeded the 24-year service credit limit of Minn. Stat. Sec. 490.121, Subd. 22.

#### 4. MSRS-Unclassified Demographic Information.

##### As of June 30, 2006:

Number of active participants .....	1,908
Average salary of active participants .....	\$62,441
Average contribution by and on behalf of participants .....	\$6,244 (\$2,498 member; \$3,746 employer)
Number of inactive participants .....	1,563
Average account balance per inactive participant.....	\$60,254
Total program assets .....	\$259,861,273

##### As of June 30, 2010:

Number of active participants .....	1,493
Average salary of active participants .....	\$70,537
Average contribution by and on behalf of participants .....	\$7,759 (\$3,527 member; \$4,232 employer)
Average account balance per active participant.....	\$107,377
Average age of active participants .....	48.1 years
Average service of active participants .....	11.3 years
Number of inactive participants .....	1,705
Average account balance per inactive participant.....	\$53,559
Total program assets .....	\$253,388,000

##### As of June 30, 2014:

Number of active participants .....	1,172
Average salary of active participants .....	\$79,236
Average contribution by and on behalf of participants .....	\$9,112 (\$4,358 member; \$4,754 employer)
Average account balance per active participant.....	\$142,258
Average age of active participants .....	45.8 years
Average service of active participants .....	10.3 years
Number of inactive participants .....	2,441
Average account balance per inactive participant.....	\$65,046
Total program assets .....	\$325,737,000

5. Plan Governance and Administration. An 11-member board of directors, the Minnesota State Retirement System (MSRS) board of directors, chaired by a board member elected from its membership, performs the policymaking function of MSRS-Unclassified. The MSRS administrative staff and the Minnesota State Board of Investment carry out the general administration or investment of the Unclassified Program. The MSRS staff, with 100 employees in 2012, executes the recordkeeping and the communication functions of the plan. The State Board of Investment and its staff perform the investment function of the plan. As of 2012, the State Board of Investment is supported by 22 staff members, two consultant firms, two custodian banks, and a 17-member Investment Advisory Council to advise the board and its staff on investment-related matters.
6. Contribution Rates and Collection. Statute requires that the employee contribution rate to the Unclassified Program must match the employee contribution rate to MSRS-General, which is currently 5% of gross salary, except for the long service judges covered by the Unclassified Program, where the member contribution is 8% of salary. In addition, the employer must contribute 6% of the employee gross salary, except for the long service judges covered by the program, where there is no employer contribution to the Unclassified Program. Employee and employer contributions, which are not taxable, are deducted or collected each payroll period and credited to the employee's account each month. The contributions generally are collected electronically by MSRS. An 8.5% fee applies for a late collection or payment.
7. Administrative Expenses. All administrative and investment expenses are borne by participants, who are charged a fee based on the size of their individual account (\$12 annually for an account balance under \$10,000, \$24 annually for an account balance between \$10,000 and \$50,000, and \$36 annually for an account balance over \$50,000) on contributions made after July 1, 1992. The 2011 program administrative expenses were \$174,000, or \$53.23 per active or inactive participant, compared to 2011 MSRS-General administrative expenses which were \$6,064,000, or \$60.85 per active, retired, or inactive participant.
8. Plan Investments. The plan investments are directed individually by each participant, who makes the actual choice in the composition of investment securities in the person's own account in the Minnesota Supplemental Investment Fund, a functional equivalent of a family of mutual funds. Under Minnesota Statutes, Section 11A.17, the investments are shares in one or a combination of the income share account, the growth share account, the international share account, the money market account, the bond market account, the fixed interest account, and the common stock index account. The contributions are invested within the month they are received. Actual investments are done through outside vendors who enter into competitively bid contracts with the State Board of Investment for five years. The contracts are reviewed periodically by the State Board of Investment.
9. Plan Communication, New Member Processing and Benefit Counseling. MSRS provides information to plan members through three newsletters each year, a quarterly benefit statement, a plan handbook, and financial reports each year. MSRS also presents to every new member a welcome letter, forms for membership, and the plan handbook. Finally, for an employee approaching retirement, MSRS provides an estimate of the person's benefit, the tax impact on the benefit if the participant either opts for a lump sum payment or an annuity. An annuity is purchased from the MSRS-General Plan fund using the accumulated balance of the participant's account. An annuity may be purchased at age 55 or older.
10. Transfers from Prior Defined Benefit Plans to MSRS-Unclassified. Minnesota Statutes, Section 352D.12, a provision of MSRS-Unclassified law, permits an MSRS-Unclassified Program participant with prior service in MSRS-General, the Correctional Employees Retirement Plan of the Minnesota State Retirement System (MSRS-Correctional), the General Employee Retirement Plan of the Public Employees Retirement Association (PERA-General), the Teachers Retirement Association (TRA), one of the first class city teacher retirement fund associations, or the Minneapolis Employees Retirement Fund (MERF), to transfer the prior member contributions and an equivalent amount of employer contributions, plus interest, from the defined benefit plan to MSRS-Unclassified. MSRS-Unclassified Program participants who had taken a refund from a defined benefit plan are also permitted to repay that refund and transfer the refund amount and equivalent employer contributions, plus interest.

Minnesota Statutes, Section 352D.12, was initially enacted in 1985 (1<sup>st</sup> Spec. Sess. Laws 1985, Ch. 7, Sec. 9). The 1985 provision was a simpler version of the current statutory provision. The 1985 provision was the last surviving provision of a broader proposed 1985 reformulation of the MSRS-Unclassified Program contained in 1985 Session S.F. 489 (Moe, D.M.) and 1985 Session H.F. 740 (Simoneau), which would have expanded the membership of the MSRS-Unclassified Program to include court employees other than judges, all Metropolitan Council employees other than MTC bus drivers and MWCC tradesmen, local elected officials earning at least \$2,400 annually, elected county attorneys and their deputies, and employees of the League of Minnesota Cities, the Association of Minnesota Counties, the Metropolitan Inter-County Association, and the Minnesota Municipal Utilities Association, would have limited the ability of MSRS-Unclassified Program participants to elect an MSRS-General retirement annuity in lieu of an MSRS-Unclassified Program benefit, and permitted the transfer of past defined benefit plan contribution accumulations to the MSRS-Unclassified Program. The proposed MSRS-Unclassified

Program reformulation was not ultimately recommended by the Commission beyond the prior contribution transfer provision.

Minnesota Statutes, Section 352D.12, was subsequently amended in 1992 (Laws 1992, Ch. 432, Art. 2, Sec. 1; Laws 1992, Ch. 598, Art. 1, Sec. 12). The first 1992 change added a sentence to the refund repayment authorization clarifying the timing for the crediting of the refund repayment, presumably for purposes of calculating interest on the amounts for transfer to MSRS-Unclassified. The second 1992 change increased the interest payable on a refund repayment to 8.5% annual compound interest.

Minnesota Statutes, Section 352D.12, was again revised in 1998 (Laws 1998, Ch. 366, Sec. 74; Laws 1998, Ch. 390, Art. 6, Sec. 1). The identical changes, one in the State Departments Appropriations Bill and the other in the Omnibus Retirement Bill, covered the transfer of past contributions from the Legislators and Elective State Officers Retirement Plans to MSRS-Unclassified for legislators and constitutional officers newly covered by MSRS-Unclassified. Laws 1998, Chapter 366, Section 12, the State Departments Appropriations Bill, also included appropriations to cover the general fund exposure for the transfers. By 2005, the transfer language had become obsolete and was removed by First Special Session Laws 2005, Chapter 8, Article 10, Section 37.

11. Option to Return to Defined Benefit Plan Coverage. Under Minnesota Statutes, Section 352D.02, Subdivision 3, a participant in MSRS-Unclassified other than a legislator, a judge, or an elected state officer who became a state employee before July 1, 2010, with at least ten years of state service, or who became a state employee after June 30, 2010, with no more than seven years of state service, is permitted to elect to transfer coverage to MSRS-General, a defined benefit plan governed by Minnesota Statutes, Chapter 352. The MSRS-General retirement annuity is 1.7% of a member's highest five successive years average salary per year of covered service, payable in full at age 65 and reduced actuarially if the annuity commenced before age 65, with the earliest reduced benefit retirement age of 55.

Laws 2010, Chapter 359, Article 4, Section 7, clarified in the language of the law, consistent with how MSRS has long interpreted the application of the provision to legislators, elected state officers, and judges. These three groups are not permitted to transfer to MSRS-General, regardless of length of service. Regarding judges, most individuals who become judges do so relatively late in their careers. To permit a retirement benefit deemed reasonable to be generated, the Judges Plan, a defined benefit plan, has a high service accrual rate. However, when an individual becomes a judge relatively early and provides long service, that accrual rate could lead to an annuity that is a very high portion of salary. The plan has long had limits to cap benefit accrual. In 2000, the previous benefit maximum (70% of annual salary in the year immediately preceding retirement) was converted to a length of service maximum (24 years of service). If a judge continued in employment beyond 24 years, no further employee contributions or service accrual was permitted in the Judges Plan. Instead, an account is created in the MSRS-Unclassified Program for the judge, funded by employee contributions. Given this apparent intention of limiting further participation in a defined benefit plan, it would be inconsistent with that policy to permit a long-service judge to opt out of the MSRS-Unclassified Program and enter MSRS-General, another defined benefit plan. Regarding legislators and elected state officers, the Legislature decided in 1997 that defined contribution coverage, rather than defined benefit coverage, was appropriate for elected officials. In 1997, as part of major benefit increase legislation assembled by MSRS, the Public Employees Retirement Association (PERA), and TRA, retirement coverage for all newly elected legislators and for sitting legislators who elected to change coverage was provided by MSRS-Unclassified. A comparable change was made for state constitutional officers. The legislation (Laws 1997, Ch. 233, Art. 2) also added Social Security coverage for legislators and constitutional officers and included a required study by the Legislative Commission on Pensions and Retirement of the appropriateness of the coverage change (see Laws 1997, Ch. 233, Art. 2, Sec. 16.) The Commission completed the mandated study during the 1997-1998 Interim and concluded that the change was appropriate and recommended no change in the 1997 coverage change.

The defined benefit plan coverage election authorization in the MSRS-Unclassified Program allows various MSRS-Unclassified Program participants to adversely select or elect against the MSRS-General pension plan, with a significant potential benefit gain for the participant and a significant potential risk of the creation of an unfunded actuarial accrued liability in the MSRS-General Plan. The option to transfer coverage from the MSRS-Unclassified Program to defined benefit plan coverage by MSRS-General has an actuarial cost for MSRS-General. The normal cost under the MSRS-General defined benefit plan for the MSRS-Unclassified active participants as of July 1, 2010, was 11.52% of covered pay, compared to the normal cost for MSRS-General active members as of the same date of 7.77% of covered pay, which is a difference of 3.75% of covered pay.

12. Summary of Program Coverage Inclusion Changes.

- In 1971 (Laws 1971, Ch. 604, Sec. 2), as part of the initial enactment of the retirement program, the coverage of the program as an alternative to the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General) included full-time employees of the Governor,

Secretary of State, State Auditor, State Treasurer in the unclassified service; full-time employees of the State Board of Investment in the unclassified service, any department division or agency head in the Executive Branch, a deputy or employee listed in Minnesota Statutes, Chapter 15A; and permanent full-time unclassified legislative employees.

- In 1973 (Laws 1973, Ch. 624, Sec. 3), the full-time requirements for employees of the constitutional officers or State Board of Investment were eliminated, employees of the Lieutenant Governor, Attorney General, and Revisor of Statutes were added to coverage eligibility, and part-time legislative employees with an account in the Minnesota Supplemental Investment Fund, whether or not eligible for MSRS-General coverage, were added to coverage eligibility, and assistant department heads were added to coverage eligibility.
- In 1976 (Laws 1973, Ch. 329, Sec. 11), the 1973 inclusion of assistant department heads was clarified as the assistant department head, but any state employee classified under statute at the deputy or assistant department, agency head, or director level were included in memberships eligibility, and the chair, chief administrator and nine upper management level employees at the Metropolitan Council or the Metropolitan Waste Control Commission were included in membership eligibility.
- In 1977 (Laws 1977, Ch. 429, Sec. 17), the executive director, assistant executive director, and nine upper management employees of the higher education coordinating board in the unclassified service were included in membership eligibility.
- In 1980 (Laws 1980, Ch. 607, Art. 14, Sec. 37), the department head and deputy or assistant department head inclusions were restructured grammatically without apparent substantive effect, the part-time legislative employee inclusion was revised to apply only to temporary legislative employees, and acting department heads were included in membership eligibility.
- In 1981 (Laws 1981, Ch. 224, Sec. 68), the Minnesota Supreme Court clerk was included in membership eligibility.
- In 1982 (Laws 1982, Ch. 399, Sec. 1), employees principally employed at the state ceremonial house were included in membership eligibility. Also in 1982 (Laws 1982, Ch. 560, Sec. 56), the chief executive officers of Department of Correction correctional facilities or Department of Welfare hospitals and nursing homes were included in membership eligibility.
- In 1983 (Laws 1983, Ch. 247, Sec. 138), the inclusion of the State Supreme Court clerk was revised as the clerk of the appellate courts.
- In 1984 (Laws 1984, Ch. 619, Sec. 14), employees of the Minnesota educational computing corporation were included in membership eligibility. Also in 1984, (Laws 1984, Ch. 654, Art. 2, Sec. 124), employees of the World Trade Center board were included in membership eligibility.
- In 1985 (1st Spec. Sess. Laws 1985, Ch. 10, Sec. 88), the chair, the executive director and the top three division directors of the Regional Transit Board, and the chief administrator of the Metropolitan Transit Commission were included in membership eligibility.
- In 1986 (Laws 1986, Ch. 458, Sec. 7), the chancellor, the state university presidents and the unclassified service managerial employees of the Minnesota State Colleges and Universities System (MnSCU) were included in membership eligibility.
- In 1990 (Laws 1990, Ch. 570, Art. 4, Sec. 1), employees of the State Lottery covered by the managerial employment plan were included in membership eligibility.
- In 1991 (Laws 1991, Ch. 317, Sec. 1), employees who participated in the program were authorized to continue in that coverage upon subsequent employment in an unlimited, full-time, unclassified position in state employment.
- In 1992 (Laws 1992, Ch. 446, Sec. 3-4), the inclusion of higher education coordinating board employees and MnSCU upper management employees was modified to accommodate an alternative election of the MnSCU-Individual Retirement Account Plan (MnSCU-IRAP).
- In 1993 (Laws 1993, Ch. 239, Art. 1, Sec. 1-3), employees of the higher education board and acting, temporary or interim upper MnSCU management employees were included in membership eligibility as an alternative to MnSCU-IRAP coverage.
- In 1994 (Laws 1994, Ch. 628, Art. 1, Sec. 3, and Art. 3, Sec. 30), the inclusions for the Metropolitan Council were revised, with coverage for the chair of the Metropolitan Council eliminated, and re-specified for the Metropolitan Council, regional administrator, executive director, general counsel, division director, operation managers, and other positions up to a total of 27 positions.
- In 1995 (Laws 1995, Ch. 141, Art. 14, Sec. 2), the 1992 inclusions related to the State Board of Technical Colleges and the Higher Education Board were eliminated and the 1994 removal of the chair of the Metropolitan Council was revised, re-including the Metropolitan Council chair in membership eligibility.

- In 1997 (Laws 1997, Ch. 233, Art. 2, Sec. 3), constitutional officers and legislators who were first elected after July 1, 1997, or who were elected before July 1, 1997, and elected the coverage were included in membership coverage.
- In 2000 (Laws 2000, Ch. 260, Sec. 56; Ch. 457, Sec. 7-8; and Ch. 461, Art. 3, Sec. 3 and Art. 18, Sec. 1), the inclusion of employees of the World Trade Center board was eliminated, the requirement for inclusion that legislative employees be permanent was replaced with the condition that legislative employees be appointed without a duration limit on that employment, the requirement that changes from the initial designations of Metropolitan Council employees included be made only with the approval of the MSRS board of directors, and judges with judicial service in excess of the Judges Retirement Plan service credit maximum were mandated post-service credit limit inclusion in the program.
- In 2002 (Laws 2002, Ch. 379, Art. 1, Sec. 77), a reference to the State Lottery was clarified by eliminating the specification of “board.”
- In 2006 (Laws 2006, Ch. 271, Art. 10, Sec. 32), an obsolete reference to the 1997-1998 election of retirement coverage by constitutional officers or legislators was eliminated.
- In 2007 (Laws 2007, Ch. 54, Art. 5, Sec. 7; and Ch. 134, Art. 2, Sec. 10), the state court administrator and the judicial district administrators, employees of the Agricultural Utilization Research Institute, employees of Minnesota Technology Incorporated, MnSCU faculty or unclassified administrators with pre-1995 employment by the state university system or state community college system and pre-1995 MSRS-Unclassified coverage, and pre-1995 state employees who are employed by MnSCU as unclassified service administrators were included in membership eligibility, and the inclusion of employees of the Minnesota Educational Computing Corporation was eliminated.