The Comparability Of Pension And Other Post-Retirement Benefits Between Public Sector And Private Sector Employees

A Report Mandated By Laws Of Minnesota 1999, Chapter 250, Article 1, Section 2, Subdivision 4

Legislative Commission on
Pensions and Retirement

January 15, 2000

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January 15, 2000

Representative Steve Sviggum
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100 Constitution Avenue
St. Paul, MN 55155-1206

Senator Allan H. Spear
President of the Senate
120 Capitol
75 Constitution Avenue
St. Paul, MN 55155-1606

Re: Letter of Transmittal for Commission Report

Dear Representative Sviggum and Senator Spear:

Herewith transmitted is a report on the comparability of pension and other post-retirement benefits between public sector and private sector employees.

The report was mandated by Laws 1999, Chapter 250, Article 1, Section 2, Subdivision 4.

The Commission hopes that this report provides useful information to the Legislature.

Sincerely,

Harry

Harry Mares
Representative, District No. 55A
Chair, Legislative Commission on Pensions and Retirement

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Executive Summary

Study Approach

The Legislative Commission on Pensions and Retirement conducted a comparison of pension and post-retirement benefit coverage between public sector employees and private sector employees by reviewing recent relevant retirement benefit coverage literature and by assembling the results of calculated hypothetical retirement annuities from various Minnesota public sector and private sector retirement arrangements requested to provide information by the Commission.

Review And Summary Of Pension Benefit Practice Literature

- Pension Benefit Coverage Is A Well-Established Part Of Employment Compensation.

  While pension benefit coverage has grown as part of employment compensation, its provision is probably based in employer managerial decisions to gain specific employment goals and in employer responses to broader societal views. Employer-sponsored pension plans began in the public sector in 1857 and in the private sector in 1875, and now cover one-half of the civilian non-agricultural workforce or more. The number of employer-sponsored pension plans has increased to more than 700,000 plans, with most of the pension plans in the private sector.

- Pension Benefit Coverage Is Most Common For Governmental Employees And Full-Time Private Sector Employees

  Pension plan participation has also grown to 84 million employees, with the greatest participation among governmental employees, sizable participation among full-time private sector employees, and the least participation among part-time private sector employees.

- Historically Predominant Defined Benefit Plan Approach Shifting To Defined Contribution Plan Approach

  Defined benefit pension plans have historically predominated, and continue to predominate, in the public sector. That same pattern generally holds true for the largest private sector employers. For smaller private sector employers and for supplemental pension coverage for larger private sector employers, defined contribution pension plans are significant in number and are growing. In total, there are 12 times more private sector defined contribution pension plans than there are private sector defined benefit plans. Although there are substantially more defined contribution pension plans than defined benefit pension plans, the concentration of defined contribution plans in small employers and the concentration of defined benefit plans in large employers translates into comparable total numbers of plan participants.

- Defined Contribution Plan Growth Due To Changing Economic Factors And Perceptions

  Defined contribution plans have become prevalent in the private sector for a variety of factors and perceptions, including changing federal tax code regulation, ease of administration, increased benefit portability, lower employer cost, and the predictability of future employer funding levels.

- Part-Time Employees And Employees Of Small Private Sector Firms Continue To Lack Pension Coverage

  Among part-time employees and for small private sector employers (under 100 employees), especially non-unionized employers in the service or retailing industries, pension coverage becomes less frequent. Uncertain business revenue, high employee turnover, lack of employee interest, pension plan administrative costs, and governmental regulatory burdens are the reasons cited for a lack of pension coverage.

- Interest In Defined Contribution Plans By Government Sector Growing

  Governmental employers are beginning to consider the creation of defined contribution pension plans, in order to appeal to older workers, part-time employees, and employees seeking flexible benefit coverage, and in order to implement greater pension portability, but the shift to defined contribution pension plans in the public sector remains slow.

- Out-Transitioning Remains Optimal Defined Benefit Plan Function

  Defined benefit plans attempt to address benefit adequacy concerns and function to remove older or less efficient employees from the workforce in a humane or socially-responsible manner, although these plans risk the creation of unfunded pension liabilities and future funding burdens and are not portable if employees become mobile.

- Employee Flexibility And Self-Reliance Are Optimal Defined Contribution Features

  Defined contribution plans allow for greater individual responsibility in saving for retirement, investing, and handling distributions, are better in providing pension portability, better control employer pension cost, and are less expensive to administer. Participants in defined contribution plans may not make adequate member contributions, may be unduly conservative in their investment practices, and may use plan accumulations for purposes other than retirement.

- Public Sector And Private Sector Relative Generosity Difficult To Quantify

  While there are considerable differences in quantifying the relative generosity of public and private sector employment compensation and benefit practices, commentators generally agree that compensation costs are greater in the public sector than in the private sector. Commentators frequently point to the differences in the occupational mix between the public and private sectors, among other factors, to explain the data differences.

- Growing Response To Demands For Earlier Retirement Ages

  Although age 65 is the historical age for the beginning of retirement, as a surrogate for determining worker incapacity and loss of productivity, a retirement lifestyle has developed in recent decades, many workers seek to retire at ages earlier than age 65, and that employers have accommodated that desire by permitting retirement before age 65.

- Typical Private Sector Defined Benefit Plan Provides Adequate Retirement Benefit

  Retirement benefit adequacy is the receipt of a benefit that replaces pre-retirement income in the range of 60-70 percent and the typical private sector defined benefit plan and Social Security will provide an adequate benefit at age 62 or age 65.

- Retiree Health Coverage Is Growing Benefit Practice

  Retiree health benefit coverage is a need resulting from earlier retirement and growing life expectancies and employers are increasingly accommodating this need with partially or wholly employer-funded medical care benefit coverage for retirees.

<u>Comparison Of Calculated Minnesota Pension Plan Hypothetical Benefit Amounts</u>

- Minnesota Larger Employer Pension Practices Parallel Identified Recent National Trends

  In a sampling of 47 Minnesota retirement benefit arrangements of large employer, largely white collar employees, local pension practice parallels the trends identified in the literature review. Defined benefit plans are the most prevalent type of pension coverage, although most of these arrangements include defined contribution plan coverage. Based on benefit amounts, the defined benefit plans provide the most significant amount of total benefits, although the defined contribution benefits can be significant. Employee and employer contribution practices vary. A majority of retirement arrangements did not provide post-retirement adjustments, did not recognize service previously covered by another pension plan, infrequently or never offered early retirement incentives, and did not provide pre-retirement benefit counseling. The employer is the most common source of the payment of pension administrative costs. Most retirement arrangements also did not provide post-retirement medical insurance coverage that was wholly or partially subsidized by the employer.

Introduction

Laws 1999, Chapter 250, Article 1, Section 2, Subdivision 4, requires the Legislative Commission on Pensions and Retirement to undertake a comparison of pension and other post-retirement benefits between public sector employees and private sector employees, with a report due on January 15, 2000.

Specifically, the appropriations rider language provides the following:

> The legislative commission on pensions and retirement shall study and report to the legislature by January 15, 2000, on the comparability of pension and other post-retirement benefits between public sector and private sector employees. When comparing the benefits, the commission shall select comparable job classifications and salary ranges. The study must compare pension portability, initial monthly benefits, average annual benefit increases, employer and employee contribution rates, availability of early retirement incentives, administrative costs, and other factors as necessary to compare benefits.

In conducting the study, the Commission combined two approaches, which are a review and summary of relevant retirement benefit coverage literature and a comparison of calculated hypothetical retirement annuities for various Minnesota public sector and private sector employers.

The literature review and summary portion of the study is based on various readily available published comparisons of public and private sector employee benefit coverage, including the employment benefit comparisons prepared by the Bureau of Labor Statistics of the U.S. Department of Labor. The literature review and summary results, involving 108 sources, are generally indicative of the benefit practices among general employer-sponsored defined benefit and defined contribution pension plans. The aim of the summary and review is to identify the characteristics of the public and private sector pension plan and retirement benefit coverage systems so that a useful comparison can be drawn with the Minnesota general employee public pension and retirement benefit coverage system.

The comparison of calculated hypothetical benefit amounts is based on the calculations of hypothetical benefit amounts and related information for the General State Employees Retirement Plan of the Minnesota State Retirement System (MSRS-General), the Public Employees Retirement Association (PERA), those members of the Minnesota Business Partnership who responded to a request for information from the Commission, and by third-party pension plan administrators located in the Twin City metropolitan area who also responded to a request for information from the Commission. The comparisons are hoped to be generally indicative of the relative generosity of various public and private sector retirement benefit arrangements and to provide some sense of context for future Minnesota public pension plan decisions by the Legislature.

Review And Summary Of Pension Benefit Practice Literature

A. Reasons For Providing Employees With Retirement Income.

Over time, retirement plans have become a part of actual or potential employment benefit practice. Employers have added pension and other benefit plans to their compensation arrangements, although the reason for doing so is not necessarily clear and must be inferred.

Marc Twinney, a pension practitioner, suggests that employers have five reasons for providing retirement income. The employer goals identified by Mr. Twinney for retirement plans are post-retirement employee security (need to replace pre-retirement income), competition (matching or exceeding competitor benefit practices), internal equity (tailoring compensation within employee segments), desired behavior inducement (rewarding employment behavior that advantages the employer), and employee choice (permitting greater employee flexibility).

Historically, retirement income is viewed as relying on a three-legged stool of financial support, consisting of Social Security, a supplementing employer-sponsored pension plan, and personal savings. Sylvester Schieber observes that there are great current concerns about the stability of the pension system in the United States, especially with potential changes in Social Security benefits and funding. Mr. Schieber also suggests that the three-legged stool of retirement income has legs that are too short for the height of the retirement table.

In reviewing the evolution of defined benefit plans, Patrick Seburn indicates that it is a societal decision that workers should enjoy adequate income in their retirement years.

The ERISA Industry Committee contends that employer-sponsored pension plan coverage and participation is concentrated among those workers who are most likely to need benefit coverage beyond Social Security benefits in order to retire (i.e., older workers and higher compensated employees), that private sector employer-sponsored pension plans provide benefits that would otherwise be sought from the government at a higher cost to employers, and that pensions are a valuable management tool, allowing the employer to attract and retain employees, to motivate employees, to allow for the out-transitioning of workers at the end of their normal career, to utilize a cost-effective compensation mechanism, and to utilize a useful mechanism to meet workforce goals.

B. Development of Public and Private Sector Pension Plans

Although the first public pension plans recognized nationally were the New York Police Pension Plan, established in 1857, and the New York City Teachers Retirement Plan, established in 1869, New York City police officers and firefighters established mutual benefit associations, funded wholly from member dues, as early as 1792. The first Minnesota public pension plan was the Minneapolis Fire Department Relief Association, established as a survivorship and disability benefit plan in 1868. Police officer and firefighter pension plans typically date to the later 1800s, when, according to Michael Bucci, police and fire employment became less patronage driven and more professional and permanent. Massachusetts established the first state general employee retirement plan in 1911. The first Minnesota statewide pension plan was the predecessor to the Teachers Retirement Association (TRA), established in 1915. Although the federal government provided pension to veterans of various wars, including the Civil War (1861-1865), the federal government did not establish the federal Civil Service Retirement System until 1920.

The first nationally recognized private sector pension plan was established by the American Express Company in 1875, although the first profit sharing plan, which could be used for retirement income purposes, was established in 1794 by the Gallatin Glass Works in Pennsylvania. The earliest private sector pension plans occurred among railroads, banking and public utilities, according to Patrick Seburn. He also reports that pension plans developed later among manufacturing industries when it became a competitive necessity. Before 1920, among private sector employers, Mr. Seburn indicates that the pension plans really were hardship payments and employer charity, since there were salary caps, employer approval was necessary in order for an employee to retire, the plan was wholly discretionary with the employer, and the plan benefits were subject to employer change at will.

Edward M. Coates indicates that profit sharing plans were utilized by private sector employers in the early 1900s to discourage unionization by their employees, but those plans rarely survived the Great Depression.

Pension coverage has become increasingly important as a component of employment compensation since World War II. Pensions first became accepted as a collective bargaining item in 1948, with a ruling from the National Labor Relations Board that pensions were included in the phrase “terms and conditions of employment,” and in 1949, with the Supreme Court decision in the Inland Steel case.

C. Coverage By Public And Private Pension Plans

Observers differ in their assessment in the extent of coverage by public and private pension plans. According to Gregory Conko, in 1979, 50 percent of the civilian non-agricultural workforce was covered by an employer-sponsored pension plan and in 1993, plan coverage dropped to 47 percent. Mr. Conko reports that in 1993, for private sector firms with at least 100 workers, 83 percent had established a retirement plan, while the figure drops to 19 percent when the private sector firm had no more than 25 workers. Yung-Ping Chen indicates that 57 percent of the U.S. workforce was employed in a business where a pension plan is established or sponsored. The Congressional Budget Office reports that, in 1993, 60 percent of the civilian non-agricultural workforce had access to employer-sponsored or union pension plans.

William Wiatrowski indicates that in 1989-1991, one-half of workers have an employer-sponsored pension plan, with almost 100 percent of public employees covered, 80 percent of full-time private sector employees of medium and large employers covered, and 40 percent of full-time private sector employees of small employers covered.

Ann Foster reports that 60 percent of all employees have coverage by at least one pension plan, with 41 percent of all employees having coverage by defined benefit plans and 31 percent of all employees having coverage by defined contribution plans (savings, thrift and deferred profit sharing plans being the most prevalent defined contribution plans). Ms. Foster indicates that almost 90 percent of public sector employees are covered by a pension plan, compared to 54 percent of private sector employees.

D. Number Of Private And Public Sector Pension Plans

The total number of private sector pension plans has increased over time. The Employee Benefit Research Institute (EBRI) indicates that there were 311,094 private sector pension plans in 1975. In 1997, EBRI estimates that the number of private sector pension plans had grown to 700,000. In 1998, Olivia Mitchell reports that there were 702,097 private sector pension plans.

The number of state and local government pension plans over time is difficult to ascertain, but available information indicates that the number is relatively constant over time and totals only one-half to one percent of the number of private sector pension plans. Ping-Lung Hsin reports that, in 1995, public pension plans had almost $1 trillion in plan assets, about the same amount as private sector pension plans, and covered 13 million active members.

E. Participation In Public And Private Sector Pension Plans

Participation in pension plans has grown, but that growth has not been even among subgroups within broad types of pension plans.

Public employee pension plans typically do not have any participation requirements, according to Ping-Lung Hsin, and as a consequence, participation in public employee pension plans is very high.

The Employee Benefit Research Institute (EBRI) indicates that private sector pension plan membership has grown from 45 million participants in 1975 to 84 million participants in 1997. Pension plan participation varies, depending on full-time or part-time employment, depending on the size of the employer, and depending on the compensation of the employee. EBRI reports that, in 1993, 78 percent of full-time private sector employees were covered by a retirement plan, while 40 percent of part-time private sector employees had retirement plan coverage. By comparison, according to EBRI, in 1994, 96 percent of full-time state or local government employees were covered by a retirement plan and 58 percent of part-time state or local government employees had retirement plan coverage. Comparing small private sector employers and larger private sector employers, EBRI found, for 1993, that of the 5.3 million small employers, defined as 100 employees or fewer, only 9 million employees of the total 38 million employees, or 23.7 percent, had retirement plan coverage.

The Government Accounting Office indicates that pension plans are available to 75 percent of full-time employees of private sector establishments with more than 100 employees, and about 50 percent of full-time employees of private sector establishments with less than 100 employees.

Compensation levels also produce different participation patterns, with Gregory Conko reporting, for 1993, that 83 percent of private sector employees making $50,000 or more were retirement plan participants, while only 28 percent of total private sector employees were retirement plan participants. Yung-Ping Chen observes that pension plan coverage is less prevalent in service sector employment, low-paying jobs, and part-time employment.

With respect to Internal Revenue Code Section 401(k) plans, a primary type of defined contribution plan, James Poterba has concluded that plan eligibility increases with employee income, but is not strongly related to employee age. Mr. Poterba also indicates that plan participation grows with increased eligibility and income, and that participation is persistent once it occurs.

Participation in supplemental private sector thrift and savings defined contribution plans is more likely, according to William Wiatrowski, because private sector employees rarely are required to make member contributions to the employer’s primary retirement arrangement. Mr. Wiatrowski also concludes that job tenure and pension coverage are correlated because of participation requirements that are frequently found in private sector pension plans.

F. <u>Types Of Pension Plans And Changes In Prevalence Over Time</u>

The public sector and the private sector differ in the type of pension plan (defined contribution plan or defined benefit plan) that predominate and the shift in plan type utilized over time. Pension plans are classified as defined contribution plans or defined benefit plans depending on which of two factors (funding requirements and benefit payouts) are fixed and which are variable. In a defined contribution plan, the funding of the pension plan is fixed and the eventual benefits payable from the plan will vary depending on the magnitude of past pension contributions, their timing, the amount of investment income earned on the accumulated contributions, and the age at which the retiree commences the receipt of benefits. In a defined benefit plan, the benefits payable from the plan are specified in some manner (frequently as a percentage of final average income per year of service) and the funding will vary depending on the generosity of the benefit plan, the demographics of the plan participants, and the actuarial assumptions formulated on economic and demographic focus.

The Employee Benefit Research Institute (EBRI) indicates that most state and local government retirement plans have been and continue to be defined benefit plans, with 95 percent of full-time state or local government employees covered by a defined benefit plan.

Jerline Thompson, summarizing data assembled by the U.S. Department of Labor, Bureau of Labor Statistics, indicates that 93 percent of state and local government full-time employees and 63 percent of private sector full-time employees are in defined benefit plans, while 53 percent of private sector full-time employees and nine percent of state and local government full-time employees are in defined contribution plans.

EBRI notes that defined contribution pension plans predominate in the number of retirement plans in the private sector and that defined contribution pension plans in the private sector have grown in number and proportion over time, as follows:

Year	Private Sector Defined Benefit Plans	Private Sector Defined Contribution Plans
1975	103,346 (33.22%)	207,748 (66.78%)
1997 (est.)	53,000 (07.57%)	647,000 (92.43%)

The Government Accounting Office (GAO) indicates that over the period 1984-1993, the number of private sector defined contribution pension plans increased from 455,000 to 565,000. In 1993, GAO reports that 88 percent of private employers with single employer pension plans were defined contribution plans, up from 68 percent in 1984. Over the 1984-1993 period, GAO reports that private employers offering only defined benefit pension plans decreased from 24 percent to nine percent. Vickie Bajtelsmit reports that most new private sector pension plans are defined contribution pension plans.

In assessing the growth of private sector defined contribution plans, Kelly Olson and Jack VanDerhei report that private sector defined benefit pension plan participants increased from 33 million in 1975 to 40 million in 1983 and has remained at the 39-41 million participant level since 1983, while private sector defined contribution plans increased in participants from 12 million in 1975 to 44 million in 1993. They further note that private sector defined benefit plans with 10-24 participants decreased 55 percent over the period 1985-1993 and that private sector defined benefit plans with 500-999 participants decreased 22 percent over the same period. Ms. Olson and Mr. VanDerhei also indicate that for single employer private sector pension plans with 100 or more participants, employee contributions to defined contribution plans increased as compared to those to defined benefit plans at a quarter rate than can be explained by employment shifts since 1985. They report that, over the period 1975-1998, private sector defined contribution plans grew in number from 208,000 to 619,000, while private sector defined benefit plans decreased in number from 103,000 to 84,000.

In comparing types of pension plans and differences between the public sector and the private sector, Ann Foster reports that 83 percent of public sector employees have defined benefit plan coverage, compared to 34 percent of private sector employees, and that 35 percent of private sector employees have defined contribution plan coverage, compared to eight percent of public sector employees.

James Poterba suggests that the 1980s were the primary period for the growth of defined contribution plans, following the authorization of Internal Revenue Code Section 401(k) plans in 1978. In 1983, he observes, there were 1,700 Section 401(k) plans, covering 4.4 million participant, growing to 83,300 Section 401(k) plans, covering 17.3 million participants, in 1989.

In the private sector, EBRI reports, this growth in the number of defined contribution plans had also impacted on the proportion of members in each type of plans, with the number of defined benefit plan members growing from 33 million in 1975 (73 percent of the total) to 40 million in 1997 (48 percent of the total), while the number of defined contribution plan members grew from 12 million in 1975 (27 percent of the total) to 44 million (52 percent of the total). Most private sector defined contribution plans are profit sharing plans or salary reduction savings/thrift plans. Olivia Mitchell provided somewhat different information on the 1998 comparison of the two major types of private sector pension plans, as follows:

Category	Total	Defined Benefit Plans		Defined Contribution Plans	
Number	702,097	84,252	(12%)	617,845	(87%)
Participants	83,900,000	40,272,000	(48%)	43,628,000	(52%)
Assets	$2,300,000,000	$1,242,000,000	(54%)	$1,058,000,000	(40%)
Contributions	$154,000,000	$52,360,000	(34%)	$101,640,000	(66%)
Benefits Paid	$156,000,000	$79,560,000	(51%)	$76,440,000	(49%)

Medium and large sector establishments, according to EBRI, are the most like state and local governments, with 72 percent of the participants in defined benefit pension plans. Mark Twinney, a practitioner rather than a theoretician, agrees that the use of defined benefit plans is declining and the use of defined contribution plans is increasing. He suggests, however, for very large private sector firms, there has been very little change in their pension practice and defined benefit plans are a significant mechanism in providing pension coverage.

G. Reasons For The Prevalence Of Defined Contribution Pension Plans In The Private Sector

Defined contribution pension plans are prevalent in some private sector establishments for a variety of reasons. The Employee Benefit Research Institute suggests that the recent prevalence of defined contribution plans is due to the large number of terminations of very small (two to nine active members) private sector defined benefit pension plans, which were previously used as tax shelters as top heavy plans, and which were adversely affected by 1982 and 1986 federal tax legislation. Ease of administration, portability of benefits, and predictability of future employer funding levels also are cited as reasons for the growth of defined contribution plans.

There is a broad perception that defined contribution plans are less costly than defined benefit plans, but Marc Twinney indicates that, in his experience as a practitioner, defined benefit plans will have a lower cost than defined contribution plans or hybrid plans (cash balance and related plans), even with equal investment performance, because the deferred vested benefit value or liability in a defined benefit plan is less than the defined contribution plan account balance for terminations before retirement age and that turnover gain will fund a significant portion of the benefits received by eventual retirees.

James Poterba suggests that Internal Revenue Code Section 401(k) plans, a primary form of defined contribution plan, play a different role in large private sector employers and small private sector employers. He believes that these 401(k) plans function as supplemental pension plans for large private sector employers, but frequently function as the primary retirement vehicle for small private sector employers.

In attempting to explain the reasons for the recent shift to defined contribution plans, Leon LaBreque suggests that the growth is due to less employer paternalism, a need for more pension portability, a desire to transfer investment risk and reward, a desire to provide greater plan flexibility, an attempt to eliminate the unfunded actuarial accrued liability of defined benefit plans, and an attempt to reduce defined benefit plan administrative expenses.

In attempting to explain the growth of defined contribution plans, Kelly Olson and Jack VenDerhei indicate that the defined contribution plan growth has been concentrated in smaller private sector firms and suggest that employers have different strategic objectives that will drive their decision for one plan type over the other. In assessing the two types of plans, Ms. Olson and Mr. VanDerhei suggest that defined benefit plans are more flexible in the timing of employer contributions and less demanding in the amount of employer contributions in rising (bull) investment markets, and defined contribution plans are more predictable in their administrative expenses and are less expensive to administer except for the smallest plans. They further suggest that defined contribution plans are growing because of governmental regulation and the associated administrative complexity of defined benefit plans, the broad employee appeal of defined contribution plans, the impact of market forces and increased global competition, and, in the public sector, taxpayer pressures.

In attempting to explain the shift of plan design predominance from defined benefit plans to defined contribution plans, William Gale and Joseph Milano indicate that this trend preceded the 1974 passage of the Employee Retirement Income Security Act (ERISA), so increased federal regulation of defined benefit plans is unlikely to be the cause of the shift.

H. Reasons For Lack Of Pension Coverage In The Private Sector

Some private sector establishments lack retirement benefit coverage. The Employee Benefit Research Institute (EBRI) suggests that the prevalence of defined contribution plans among small private sector employers or the lack of any pension coverage among small private sector employers is due to a future revenue flow that is too uncertain to commit to pension plan funding, or is because the employees of small private sector employers do not value retirement savings, or is due to employee turnover that is too great to justify the establishment of a pension plan. Additionally, EBRI cites the administrative cost of pension plan operation and the burden of governmental regulation as factors arguing against pension plan establishment.

In comparing pension plan administrative costs, Olivia Mitchell determined in 1992 that defined benefit pension plan administrative costs were between $90 - $150 per participant per year, or 11 percent - 17 percent of annual plan contributions, and that defined contribution pension plan administrative costs were $31 per participant per year for single employer plans and $97 per participant per year for multi-employer plans, or two percent - ten percent of annual plan contributions. Additionally, she found that 401(k) defined contribution pension plan administrative expenses ranged from $5 - $55 per participant per year and that public pension plan administrative expenses averaged $130 per participant per year, or nine percent of annual plan contributions.

William Wiatrowski has noted the difference in the provision of pension coverage among types of private sector employers and between full-time and part-time employees, with the greatest likelihood of pension coverage among full-time employees and in goods-producing industries and the least likelihood of pension coverage among “contingent” or part-time workers and in service or retailing industries. Mr. Wiatrowski also reports that pension coverage is least common in small businesses and in non-union employment settings.

Small business, which is defined as employers with less than 100 employees, employs slightly more than one-half of the private sector workforce according to Mr. Wiatrowski, who provides the following 1993 breakdown of private sector employers:

Number of Workers	Percentage of Employers	Percentage of Workers
Under 5 Workers	15%	7%
5-9 Workers	18	9
10-19 Workers	11	11
20-49 Workers	8	16
50-99 Workers	3	13
100 or More Workers	2	44

Mr. Wiatrowski indicates that small businesses comprise a majority of employers in almost all industry types, as follows:

Industry Type	Percentage of Small Businesses
Mining	50%
Construction	82
Manufacturing	30
Transportation/Utilities	45
Wholesale	76
Retail	72
Finance, Insurance, Real Estate	55
Services	53

I. Reasons For The Choice Of Defined Contribution Pension Plans By Private Sector Employers

Private sector establishments and their employees vary in their utilization of defined contribution plans.

Michael Bucci concludes that a prime reason for savings and thrift plans, a common form of defined contribution plan, is the provision of an additional or an alternative source of retirement income.

The National Commission on Retirement Policy indicates that, in 1996, only 21 percent of workers in private sector defined contribution plans that allow for member contributions contributed the maximum amount of the employee contribution matched by the employer. Also according to the National Commission on Retirement Policy, 25 percent of participants report that they intend to use their 401(k) pension plan accumulations for buying a house or for paying for education expenses for children rather than for retirement. Of the participants who terminate covered employment before retirement, the National Commission on Retirement Policy reports that 90 percent in 1996 did not roll their account balances over into another pension plan.

The ERISA Industry Committee identifies the strengths of defined contribution plans, which are that pension benefits are generally more portable, that pension savings are more visible to workers, that benefit coverage is easier to understand, that benefits typically accumulate more rapidly during the initial years of employment, that funding requirements can be made more predicable or are entirely within the employer’s control, that administrative costs tend to be lower, that these plans provide retirement savings opportunities that otherwise would not be available for workers of small businesses, and that these plans encourage self-reliance.

Commenting on the growth of defined contribution plans, Olivia Mitchell and Sylvester Schieber indicated that the shift to defined contribution plans is appealing because other small and medium sized employers are fleeing defined benefit plans, because defined contribution plans are currently used for supplemental plans by larger employers, because defined contribution plans generally represent total retirement plan coverage for smaller employers, because defined contribution plans are viewed as more flexible by both employers (focusing on contribution amounts and the ability to reward specific types of employees and behaviors) and employees (focusing on investment self-direction, portability, and early distribution availability), because defined contribution plans are perceived as less expensive from a contribution standpoint, because defined contribution plans have smaller per participant administrative expenses, and because defined contribution plans have an underfunding risk.

Sylvester Schieber, Richard Dunn, and David Wray indicate that some large employers are considering making a wholesale change to defined contribution plans, in part because the perceived value of a defined contribution plan pension is greater than that of a defined benefit pension with a comparable actuarial cost.

J. Reasons For Considering Defined Contribution Plans For State And Local Government Employees

Public sector employers are considering defined contribution pension plans more frequently in recent years. Cathie Eitelberg suggests that workforce developments will push state and local government pension plan developments, encouraging them to consider defined contribution plans because of a need to appeal to older potential workers and potential part-time workers and to accommodate potential employees who value flexible benefits. Eitelberg indicates that this pressure to consider different pension plan designs results from competition for workers with private sector high technology firms, because there is a pending shortfall of younger potential workers, which will particularly affect public safety employment, and because the public sector workforce has growing benefit portability concerns. Eitelberg concludes that the public sector will need to become a benefit facilitator rather than a benefit provider in the future.

Douglas Fore concurs in some of these conclusions, predicating that public pension plans will shift in the future from defined benefit plans to defined contribution plans in order to gain benefit portability and in order to accommodate older potential workers.

The Government Accounting Office reports that all states have established supplemental defined contribution plans, although only five states provide for an employer contribution to the supplemental defined contribution plan. The Government Accounting Office also indicated that 21 additional states have considered replacing their defined benefit plan with a defined contribution plan, encouraged by potential cost reductions and desired benefit portability enhancement, but did not make the change, most frequently citing special interest lobbying. The Government Accounting Office also reported that public and private sector pension plans operate in different environments, with private sector employers provided with a tax deduction for its contribution to the pension plan and with private sector pension plans subject to more comprehensive federal income tax code regulations, and with public sector pension plans subject to state legislation for their features and changes and subject to more overt political considerations.

K. Typical Defined Benefit Pension Plan Practices

Defined benefit pension plans in both the private sector and the public sector are the longest duration type of retirement coverage. Defined benefit pension plans also tend to be more complex in their benefit plan provisions.

In designing a defined benefit pension plan, Preston Barrett indicates that the intended income replacement ratio is the primary factor, with the manner of accommodating Social Security and the maintenance of affordable cost also constituting significant factors. The income replacement ratio relates to the maintenance of a pre-retirement standard of living after retirement and is the initial retirement annuity expressed as a percentage of the immediate pre-retirement final annual compensation.

Marc Twinney indicates that there are many theories about the goals for a defined benefit plan, but from a practitioner's perspective, industrial firms prefer defined benefit plans to meet their retirement objectives, valuing the plan's effectiveness over cost considerations. Mr. Twinney suggests that defined benefit plans are the best vehicle for removing older, less efficient, employees from the workforce in a humane and socially responsible way and that this out-transitioning purpose for a pension plan is more important than the pension plan's role in recruitment or retention.

In governmental defined benefit pension plans, based on a survey of 100 plans covering 10.7 million active members, the National Education Association found that Social Security coverage is not universal (about 80 percent coverage), 11 percent explicitly integrate their plans with Social Security benefits, age 60 or 62 is the most common normal full retirement benefit retirement age, all plans have an early retirement benefit with a reduction, 61 percent have a vesting period of five years or shorter, 65 percent utilize automatic post-retirement adjustments, the median member contribution rate is five percent of covered pay, final average salary plans are universal (with a three-year averaging period being the most common averaging period), and benefit accrual rates vary from under 1.5 percent of the final average salary to 3.0 percent of the final average salary per year of allowable service.

Portability is a problem for employment-mobile employees, and, as observed by Ann Foster, that the portability problem is better addressed by defined contribution plans than by defined benefit plans unless the defined benefit pension plan is a multiple employer pension plan.

The ERISA Industry Committee concludes that defined benefit plans provide several important advantages for employers and participants, with the payment of lifetime joint and spousal survival annuities, the payment of benefits guaranteed for life, the payment of benefits based on final average salary, flexible benefit formulas and benefit formulas that can be instantaneously enhanced, the ability to accrue substantial benefits over a short period of time, the provision of benefits that are insulated from cutbacks, benefits that do not require employer action, and plan operations where the sponsoring employer assumes the full investment risk and full control of plan assets.

Cognizant of the significant liabilities that can be created from the benefit levels promoted in a defined benefit plan, the need for the accurate determination of those liabilities, and the potential for problematic funding arrangements in public employee defined benefit plans, where federal law does not specify minimum funding standards, Olivia Mitchell noted the prevalent practice among public employee defined benefit plans of having actuarial assumptions set by the governing board of the pension plan and having governing board members selected in significant numbers by plan members or by the applicable employer. Similarly, Sylvester Schieber, Richard Dunn, and David Wray indicate that there are growing concerns about an aging workforce and about the funding structure of defined benefit plans.

L. Typical Defined Contribution Pension Plan Practices

Defined contribution pension plans vary in their benefit practices. Based on a sampling of 1993 data for employers with 100 or more employees who have defined contribution plans that was collected by the U.S. Department of Labor, the Government Accounting Office reports that 51 percent had age and service minimum requirements in order to participate in the plan, that 97 percent provided employer contributions, most commonly for plans without an employee contribution, that 56 percent permitted employee contributions, that a majority had vesting provisions, that there was no clarity about the ability to self-direct individual account investment, that almost 67 percent permitted borrowing individual account assets or withdrawing individual account assets before retirement, and that almost all plans permitted a lump sum distribution of plan benefits. The Government Accounting Office also indicates that the proportion or magnitude of employer contributions to employee contributions declined from 3.8 (employer) to 1 (employee) in 1988 to 1.8 (employer) to 1 (employee) in 1993. Olivia Mitchell reports that the typical employee and employer contribution rate to defined contribution plans in 1998 was six percent of pay.

When defined contribution pension plans are the primary pension vehicle for employees, there are potential problems, As Vickie Bajtelsmit indicates, there is evidence that employees who have the opportunity to direct the investment of their own account balances are averse to investment risk, especially women, tend to select debt securities over equity investments, and will suffer from this risk aversion by experiencing lower investment returns, obtaining lower income replacement ratios, and threatening their benefit security over longer potential retired lifetimes. Ms. Bajtelsmit also suggests that lump sum distributions from defined contribution plans, a typical feature of this type of plan, are not being properly invested. She additionally indicates that with the growth of defined contribution plans and with the shift of the burden of retirement planning form employers to individual employees, investment performance may influence the employee's retirement date, which carries implications for the employer because the delayed retirement date may cause outtransitioning problems. similarly, Marc Twinney suggests that when defined contribution plans replace defined benefit plans, the change will appear to be more valuable to younger employees, but the change may induce older employees to delay their retirement. This may actually result in no cost savings for the employer, since the defined benefit plan will produce a net savings if retirement is delayed for one year, but there is no defined contribution plan savings in the same circumstance. A delay in beginning a defined benefit plan retirement annuity will reduce the period of benefit receipt and produce an actuarial gain (liability release), but the same delay for a defined contribution plan leaves the same value in the participant account.

Olivia Mitchell and Sylvester Schieber identify a concern about defined contribution plans, which is the shift of investment risk and responsibility to plan participants, who may be poorly informed about long term investing. Sylvester, Schieber, Richard Dunn, and David Wray suggest that there are a number of problems with defined contribution plans, which they identify as the consequences of employers attempting to fashion cheap pension coverage in creating defined contribution plans, the susceptibility of defined contribution plans to pre-retirement distributions, the consequences of self-directed defined contribution plan investments that are more conservative than defined benefit plan investments, the consequences of the lack of participation in defined contribution plans by lower income employees, and the consequences of the lump sum payouts common among defined contribution plans.

Vickie Bajtelsmit also points out that self-directed defined contribution plans that permit or encourage the investment of participant account assets in securities of the employer may cause problems.

Michael Bucci indicates that savings and thrift plans are the most prevalent type of defined contribution plans by number of participants. The basic savings and thrift plan provisions are the requirement of an employee contribution, the specification of minimum and maximum contribution amounts, the specification of an employer match, the specification of investment of account balances, generally with participant investment choices, and the specification of payouts, generally lump sum distributions. Mr. Bucci found that a one-percent employee contribution is a typical minimum amount, a 13-14 percent employee contribution is a typical maximum, and the employer contribution is typically less than the employee contribution. Mr. Bucci also observes that different account balance amounts are caused by differences in the amount of investment income earned, differences in employee salary and contribution levels, and differences in the length of the employee service covered by the plan.

The Government Accounting Office reports that, in 1993, the administrative expense of operating a defined contribution plan was \$103 per participant, compared to \$157 per participant for a defined benefit plan. Mitchell reports in 1998 that a private sector defined benefit plan on average had administrative expenses that are 216 times greater than those of a private sector defined contribution plan, where many management expenses are excluded, although private sector defined benefit plan administrative expenses vary from \$850 per participant per year for small (15 participants) plans to \$56 per participant per year for large (10,000 participants) plans.

Comparing the administrative expenses of single employer Internal Revenue Code Section 401(k) plans, a type of defined contribution plan, and single employer defined benefit plans, Edwin Hustead found that plan administrative expenses ranged from 3.1 percent of pay for the smallest defined benefit plan to 0.23 percent of pay for the largest defined benefit plan and from 1.44 percent of pay for the smallest defined contribution plan to 0.16 percent of pay for the largest defined contribution plan. Mr. Hustead found that pension plan administrative expenses rose steadily over the 16-year period of his study, with defined benefit plan administrative expenses rising more steadily than defined contribution plan administrative expenses (because of consulting fees growing faster than inflation, of costs attributable to regulatory changes, and of Pension Benefit Guarantee Corporation plan termination insurance premium costs.

M. Cost And Relative Generosity Of Public Sector And Private Sector Employment Benefit Packages

In assessing the differences in relative generosity between public sector pension plans and private sector pension plans, William Wiatrowski suggests that these relate largely to the presence or absence of member contributions and to the presence or absence of Social Security coverage.

Public and private sectors differ in the cost and the relative generosity of their compensation and retirement benefit practices. The Employee Benefit Research Institute, for 1996, indicates that total compensation costs for state and local employment was $25.73 per hour, with benefits comprising 30.2 percent of the cost, while total compensation costs for medium and large private sector employment was $20.09 per hour, with benefits comprising 30.1 percent of the cost. The Employee Benefit Research Institute reports that these figures blend a broad composition of employees, with the state and local government employment figures including public safety employees and with the private sector employment figures including a large proportion of wholesale and retail sales and manufacturing employees. Public safety employees tend to receive the most substantial pension coverage in the public sector, while retail sales employees tend to receive the least substantial pension coverage in the private sector. In comparing federal government and private sector white collar compensation practices, the Congressional Budget Office concludes that there is no significant difference between federal and private sector salaries for employees with similar characteristics and that the federal government places employees with education, experience, and other characteristics in higher ranking/higher responsibility positions than the private sector does.

Bradley Braden and Stephanie Hyland, in comparing compensation costs between the state and local government sector and the private sector, reached somewhat different conclusions for the early 1990s. Mr. Braden and Ms. Hyland indicate for 1992 that state and local government compensation costs were $23.49 per hour (with wages totaling $16.39 per hour and with benefits totaling $7.10 per hour) while private sector compensation costs were $16.14 per hour (with wages totaling $11.58 per hour and with benefits totaling $4.55 per hour). They also argue that these are misleading figures because of the variations between the state and local government sector and the private sector in work activities, occupational structure, and pension plan participation. They note that the mix of workers differs between the two sectors, with the state and local government sector having proportionally more white collar and highly-skilled workers than the private sector. Mr. Braden provided a breakdown of the 1992 compensation costs per hour, organized by sector and occupation type, as follows:

	Private Sector		Government Sector	
Occupational Grouping	$	% of Workforce	$	% of Workforce
White Collar	$18.95	51%	$26.55	68%
Blue Collar	15.88	32	18.06	12
Service*	8.43	17	16.52	20

**Service grouping includes police and fire employment for the governmental sector*

Glenn Grossman indicates, for 1991, that employer-provided benefits equaled 30 percent of wage costs.

Thomas Burke and John Morton also attempted to assess the relative cost of employment benefit coverage, focusing on industry types rather than a public sector/private sector analysis, and found the following:

Industry Type	Cost per Hour		
1. Goods Producing			$3.71
a. Construction		$2.65	
b. Manufacturing		$3.93	
- Durables	$4.38		
- Non-Durables	$3.29		
2. Service Producing			$2.42
a. Transportation		$4.71	
b. Wholesale Trade		$3.33	
c. Retail Trade		$1.04	
d. Financial, Insurance, Real Estate	$3.46		
e. Services		$2.46	
Total			$2.78

William Wiatrowski also provides a sense of wage and benefit costs on an hourly basis, broken down for 1993 between large private sector employers (over 100 employees) and small private sector employers (under 100 employees), as follows:

Comparison Item	Large Employers	Small Employers
Hourly Wages	$13.00	$10.75
Employment Benefit Cost per Hour	$5.90	$3.95
Employer Supported Medical Insurance Coverage	83%	71%
Deferred Benefit Plan Coverage	59%	22%
Defined Contribution Plan Coverage	48%	33%

Specifically, with respect to the federal retirement programs, the Congressional Budget Office concludes that the federal government retirement plans are more generous than those of medium or large private sector employers, especially with respect to early normal retirement ages and matching thrift plan employer contributions. The Congressional Budget Office, utilizing a private actuarial firm's database that covers predominantly large firms, calculated the total benefit package for the federal government between 26 percent and 50 percent of salary, compared to the total benefit package for large private sector firms between 24 percent and 44 percent of salary. The Congressional Budget Office concluded that the federal government benefit practice generally exceeds private sector benefit practice. The Congressional Budget Office indicates that the Federal Employee Retirement System, applicable to new federal employees, has somewhat higher retirement benefits than large private sector firms, and also is somewhat more generous than the phasing-out federal Civil Service Retirement System. Additionally, the Congressional Budget Office determined that the federal government provides better retiree health insurance coverage than the large private sector firms, but that the private sector firms provide better active employee health and life insurance coverage than the federal government. The Congressional Budget Office found, on average, that federal government salaries were 22 percent lower than the private sector for similar jobs, but where there is a comparable salary, the entire federal government benefit package equals or exceeds the private sector benefit package. The Congressional Budget Office conjectured that this was not the case for higher grade employees and higher skill positions, where the total pay and benefit package of the larger private sector firms exceeds the federal government package.

The Government Accounting Office, making hypothetical benefit calculations using the same private actuarial firm database as used in the Congressional Budget Office, concluded that there was no definitive answer on the question of the relative generosity of large private sector benefit plans and that of the federal government, because the conclusion depends on the actual retirement age, the plan's normal retirement age, the extent that supplemental defined contribution plans are utilized, the impact of any benefit post-retirement adjustments, and the problems inherent in any method of comparing benefit packages.

In gauging the relative generosity of public and private sector pension plans, the Congressional Research Service determined that federal and private sector designs of pension and savings plans differed greatly, with the federal government pension plan coverage providing the beneficial features of post-retirement inflation, unreduced retirement annuities before age 62, subsidized spousal survivor protection, and a larger employer contribution to a savings plan. The Congressional Research Service indicated that, on an annualized value basis, the newly established Federal Employee Retirement System (FERS) provides 20-40 percent larger retirement benefits than the typical large private sector pension plans.

On the question of relative generosity, William Wiatrowski indicates that public sector defined benefit plans are all earnings-based plans, while only 70 percent of private sector defined benefit plans are earnings-based plans, that the typical public sector defined benefit plan benefit accrual rate is 1.9 percent of the final annual salary, while the typical private sector defined benefit plan benefit accrual rate is 1.49 percent of the final average salary, and that the differences are a function largely of this contribution effect, the Social Security effect, and the post-retirement adjustment effect. Public sector defined benefit plans typically require member contributions while private sector defined benefit plans rarely require member contributions. Public sector defined benefit plans sometimes replace Social Security coverage rather than supplement Social Security coverage, while private sector defined benefit plans always supplement Social Security coverage. Approximately one-half of state and local public employee pension plans have automatic post-retirement adjustments, while virtually no private sector pension plans have automatic post-retirement adjustments. Mr. Wiatrowski additionally indicates that it is difficult to conclude with certainty whether public sector or private sector pension plans have the most advantageous benefit coverage because of differences in the amount of member contributions and Social security coverage.

Private sector pension plans tend to integrate their coverage for Social Security coverage more frequently than public sector pension plans and, according to Avy Graham, that integration practice can reduce the cost of pension coverage to the employer.

In a defined benefit plan, pension cost at any time is a function of the generosity of the benefit plan, the specific attributes of the demographic group covered, and the actuarial assumptions and methods used to value the plan. The Congressional Budget Office reports that the federal government has a very low rate of resignations and turnover, compared to the private sector, probably because of the size of the federal government as an employer and because of the significant potential for internal employment transfers. This relative lack of turnover for the federal government would likely produce a higher employer pension cost than a private sector employment situation, even with the same benefit plan provisions.

William Gale and Joseph Milano point to a 1980 study by Samwick and Skinner that suggests that defined contribution plans are, on average, as generous as defined benefit plans.

N. Retirement Benefit Access

While age 65 may be the historically identified age for retirement, the trend is clearly for earlier access to retirement benefits among employer-sponsored pension plans, while Social Security has increased its age for the receipt of a full benefit.

Dora Costa reports that using age 65 for retirement as a surrogate for a determination of an incapacity for continued work by an employee dates to Germany in 1883 and that age 65 was designated as the retirement age for Social Security benefits in 1934, based on a number of considerations. Ms. Costa contends now that the pension plan retirement age is not now wholly a question of employee health or productivity determination, but represents economic considerations and custom. She indicates that urbanization also has played a role in the retirement experience, that older workers now have difficulty in being rehired and leaving unemployment, that a retirement lifestyle has now developed beyond dependence on family and friends, and that leisure has become an end-of-life goal of employees.

Among private sector pension plans for employers with 100 or more workers in 1989, William Wiatrowski indicates that 90 percent allowed for the payment of retirement benefits at age 55 or an earlier age and that nearly two-thirds allowed retiring employees to receive a retirement benefit without a reduction before age 65.

Growing interest in making the transition between full-time employment and retirement has been noted by Norman Jones, who reviewed deferred retirement option programs as a mechanism to assist employers in smoothing that transition for long-term employees.

O. Retirement Benefit Adequacy

The adequacy of retirement benefit coverage is frequently measured by the proportion of pre-retirement income that is replaced by the retirement benefit, known generally as the replacement rate.

As William Wiatrowski observes, retirees rarely need a 100 percent replacement of the annual pre-retirement salary because of the change in tax status, experiences and lifestyle that accompany retirement. He notes that Social Security can replace up to 40 percent of pre-retirement salary at age 65, depending upon income and declining in its replacement percentage as income increased. Mr. Wiatrowski surveyed private sector defined benefit plans of employers with 100 or more employees, where this calculation can readily be made, and calculated the following typical replacement rates of those private sector defined benefit plans, including Social Security benefits:

Age	Single Life Benefit	Joint Benefit	Survivor Benefit
55	20%	19%	10%
62	50%	60%	40%
65	60%	70%	45%

Mr. Wiatrowski also observes a trend for a greater percentage of the U.S. population to receive retirement income from employer-provided pension plans, with 55 percent of households headed by a person age 65 years or older receiving an employer-provided pension plan benefit in 1988 and expected to grow to 88 percent in 2018. A substantial contributor to this trend, according to Mr. Wiatrowski, is the greater presence of women in the workforce outside the home.

While there is no fixed standard for retirement benefit adequacy, William Wiatrowski indicates a general view that 60-70 percent of pre-retirement income is the target replacement rate. Workforce decisions and related factors can increase or decrease the likelihood of the receipt of an adequate retirement benefit, according to Mr. Wiatrowski, such as the employee's choice of employment area (employer-sponsored pension plans are most prevalent for unionized workers and in goods-producing industries), job tenure (the median job tenure for workers ages 55-64 was 12.4 years in 1991 and has declined over time), early age retirement (full-time workers are retiring at early ages and with reduced pension benefits), increased life expectancy (longer period over which to maintain purchasing power), and the lack of post-retirement inflation protection (not all retirement benefits are indexed of subject to post-retirement adjustments). Mr. Wiatrowski also indicates that defined contribution plans are less clearly oriented to meeting any pre-retirement income replacement rate, hence less clearly designed to meet adequacy goals, and tend to pay lump sum benefits, which do not encourage long term benefit adequacy.

P. Retiree Health Benefit Coverage

Retiree health benefit coverage is becoming part of employee compensation practices.

With increasing life expectancies (from age 49 in 1900 to age 81 in 1988), Dolphine Williams argues that the need for providing retiree health care benefits is growing. Ms. Williams reports that retiree health care benefits with at least some employer funding occur in 45 percent of private sector employers with 100 or more workers, in 15 percent of private sector employers with less than 100 workers, and 58 percent of state and local government employing units.

Comparison Of Calculated Hypothetical Benefit Amounts From Various Minnesota Pension Plans

A. Goal Of Requested Hypothetical Benefit Amount Comparison

In addition to undertaking a review and summary of recent literature comparing public and private sector employee benefit coverage, the Commission requested several Minnesota pension plans to provide a calculation of representative hypothetical retirement amounts and related information. The Commission hopes that a comparison of the submitted results, while not from a representative sampling and not open to generalization, will provide some sense of Minnesota private sector retirement benefit practice and its relative generosity.

B. Sampling

As suggested by the Commission staff, the sample of Minnesota pension plans from which calculated hypothetical retirement benefit amounts for comparison was intended to be drawn was to be a combination of three sources. The sources were intended to be one-quarter of the companies that are members of the Minnesota Business Partnership, the plans administered by third-party pension plan administrators in the Twin City area listed in the Minneapolis or St. Paul telephone directories, and thirty or forty representative smaller employers suggested by Commission members (three or four per legislator) from their legislative districts.

Although the Minnesota Business Partnership reviewed the hypothetical retirement benefit calculation questionnaire, the Partnership declined to provide any other assistance in this data collection process. Seven out of the twenty-six Minnesota Business Partnership businesses that were sent a survey responded to the Commission’s request as of January 6, 2000.

Information on 21 other retirement benefit arrangements was provided by third-party plan administrators, with each responding plan administrator providing calculations for more than one retirement benefit arrangement.

No Commission member suggested any smaller “Main Street” business for contacting, so no smaller Minnesota businesses from this source are included in the comparison of current retirement benefit practices.

C. Comparison of Results of Hypothetical Retirement Benefit Calculations

1. Occupational Type For Retirement Benefit Plan

Of the 47 retirement benefit arrangements compared, 11 different occupational types or combinations are identified, as follows:

Occupational Type	Number of Plans	%
Clerical	9	19.15
Clerical/Management - Supervisory	2	4.26
Executive	3	6.38
Management	3	6.38
Managerial - Supervisory	13	27.66%
Other	4	8.51
Production	5	10.64
Production/Other	1	2.13
Retail	1	2.13
Staff	4	8.51
Union	3	6.38

2. Employer Size

Of the 47 retirement benefit arrangements compared, most plans covered employers that would be considered medium or large employers (workforces over 100 employees). The breakdown is as follows:

Employer Size	Number of Plans	%
0-25	7	14.89%
26-100	3	6.38
101-1000	11	23.40
Over 1000	27	57.45

3. Retirement Age For Hypothetical Retirement Benefit Calculation

The 47 retirement benefit arrangements varied in the retirement age used in making the hypothetical retirement calculation, as follows:

Retirement Age	Number of Plans	%
49	1	2.13%
50	1	2.13
51	1	2.13
57	1	2.13
62	9	19.15
63	2	4.26
64	3	6.38
65	30	63.83

4. Years Of Employment For Hypothetical Retirement Benefit Calculation

The 47 retirement benefit arrangements also vary in the number of years of employment that the requested hypothetical typical employee would have at retirement for the purposes of the benefit calculation, as follows:

Years of Employment	Number of Plans	%
5	1	2.13
9	1	2.13
10	1	2.13
12	1	2.13
14	2	4.26
15	7	41.89
16	1	2.13
17	1	2.13
18	1	2.13
19	1	2.13
20	3	6.38
23	2	4.26
25	10	21.30
29	1	2.13
30	10	21.30
31	1	2.13
38	1	2.13
40	1	2.13
45	1	2.13

5. Final Annual Salary For Hypothetical Retirement Benefit Calculations

Of the 41 retirement benefit arrangements that disclosed a final annual salary for its hypothetical retirement calculation, there was a wide range of final salaries utilized for the calculation of a typical retirement benefit, as follows:

Final Salary Figure	Number of Plans
$20,000 - 25,000	7
25,001 - 30,000	5
30,001 - 40,000	5
40,001 - 50,000	7
50,001 - 60,000	5
60,001 - 75,000	3
75,001 - 100,000	4
Over 100,000	6

6. Defined Benefit Plan Retirement Coverage

Defined benefit plan retirement annuity coverage was the most prevalent type of retirement coverage among the 47 retirement benefit arrangements, with 40 arrangements including a defined benefit plan retirement annuity. The amount of the defined benefit plan retirement annuity varies considerably, based on differences in the generosity of the applicable benefit plan, the age of the hypothetical retiree, and the final salary of the hypothetical retiree. A comparison of defined benefit plan amounts is as follows:

Annual Defined Benefit Plan Amount	Number of Plans
Under $2,000	1
2,001 - 3,000	1
3,001 - 4,000	0
4,001 - 5,000	3
5,001 - 6,000	4
6,001 - 7,000	2
7,001 - 8,000	1
8,001 - 9,000	2
9,001 - 10,000	2
10,001 - 15,000	8
15,001 - 20,000	4
20,001 - 30,000	7
30,001 - 40,000	1
40,001 - 50,000	1
50,001 - 75,000	2
75,001 - 100,000	1
100,001 - 125,000	1

7. Internal Revenue Code Section 401(k) Retirement Coverage

Retirement coverage by an Internal Revenue Code Section 401(k) defined contribution plan was sporadic, occurring in 12 of the 47 retirement benefit arrangements. Of that 12, Internal Revenue Code Section 401(k) plan was the sole pension plan in three instances, augmented defined benefit plan coverage in whole or in part in six instances, and augmented other defined contribution plan coverage in three instances. The amount of the Internal Revenue Code Section 401(k) retirement benefits varies, as follows:

Annual 401(k) Plan Amount	Number of Plans
Under $2,000	1
2,001 - 6,000	2
6,001 - 10,000	1
10,001 - 15,000	3
15,001 - 20,000	2
20,001 - 25,000	2
20,001 - 25,000	2
25,001 - 30,000	1

8. Thrift/Retirement Savings Plan Retirement Coverage

Retirement coverage by a thrift or retirement savings plan was also infrequent, occurring in only one of the 47 retirement benefit arrangements.

9. Profit Sharing Plan Retirement Coverage

Retirement coverage by a profit sharing plan was also infrequent, occurring in six of the 47 retirement benefit arrangements. The amount of profit sharing plan benefits varies, as follows:

Annual Profit Sharing Plan Amount	Number of Plans
Under $1,000	1
1,001 - 5,000	2
5,001 - 10,000	1
10,001 - 15,000	1
15,001 - 20,000	1

10. Other Defined Contribution Plan Retirement Coverage

Retirement coverage by other defined contribution plan arrangements was infrequent, occurring in six of the 47 retirement benefit arrangements. The amount of that other defined contribution plan benefit coverage is as follows:

Other Defined Contribution Plan Amount	Number of Plans
Under $3,000	2
3,001 - 6,000	2
6,001 - 10,000	0
10,001 - 15,000	2

11. Employee Contribution To Retirement Coverage Arrangements

Only two of the 47 retirement benefit arrangements had member contributions to defined benefit plan coverage. Member contributions to Internal Revenue Code Section 401(k) plans were applicable in 19 instances, although only 12 indicated that they had Internal Revenue Code Section 401(k) plan coverage. The one thrift plan indicated member contributions and no member contributions were indicated for retirement benefit arrangements with other defined contribution plans.

12. Employer Contributions To Retirement Coverage Arrangements

The reported employer contributions to retirement coverage arrangements vary, as follows:

Reported Employer Contributions	Number of Plans
Defined Benefit Plan	15
Internal Revenue Code Section 401(k) Plan	14
Thrift/Savings Plan	1
Other Defined Contribution Plan	10

13. Post-Retirement Adjustments

Several of the 47 retirement benefit arrangements report that the plan provided post-retirement adjustments, as follows:

Post-Retirement Adjustments	Number of Plans	%
No Specific Response	3	6.38%
Ad Hoc Adjustments	17	36.17
Automatic Adjustments	2	4.26
No Adjustments	25	53.19

14. Recognition Of Service Covered By Another Plan

Portability of pension coverage in the form of the recognition of service by another pension plan did occur, with 17 arrangements (36.17%) indicating that they recognize service covered by another pension plan and 30 arrangements (63.83%) indicating that they did not recognize service covered by another pension plan.

15. Early Retirement Incentives Offered

The 47 retirement benefit arrangements reported on their practice of offering early retirement incentives, as follows:

Frequency of Early Retirement Incentive Offer	Number of Plans	%
Never	15	31.91%
Infrequently	24	51.06
Periodically	2	4.26
No Response	7	14.89

16. Payment of Retirement Plan Administrative Expenses

The 47 retirement benefit arrangements also reported on their practice of paying the administrative expenses of the retirement plan or plans, with the indicated source of those administrative expense payments as follows:

Source of Retirement Plan Administrative Expense Payment	Number of Plans	%
Employee	3	6.38%
Employer	29	61.70
Combination Employee and Employer	8	17.02
Plan Trust	6	12.77
No Response	1	2.13

17. Provision Of Employer Subsidized Post-Retirement Health Insurance Benefits

The 47 retirement benefit arrangements provided information on their practice of providing wholly or partially subsidized post-retirement health insurance or medical insurance benefits to retirees, with 16 arrangements (34.04 percent) providing subsidized post-retirement health insurance benefits and 31 arrangements (65.96 percent) not subsidizing post-retirement health insurance benefits.

18. Provision Of Pre-Retirement Benefit Counseling Services

Of the 47 retirement benefit arrangements, 11 (23.40 percent) indicated that they provide benefit counseling to employees prior to the retirement, while 36 (76.60 percent) indicated that they did not.

Conclusion

In reviewing a substantial body of relevant retirement literature, the Legislative Commission on Pensions and Retirement finds that the provision of retirement benefits as an employment benefit is a clearly established practice, with roots in the late nineteenth century, and applies to virtually all public sectors employees and 60 percent of private sector employees. It found that in excess of 700,000 private sector pension plans and a few thousand public sector pension plans have been established, covering some 97 million active members.

Pension plans have been classified as either defined benefit plans or defined contribution plans, and the Commission found that there has been a shift from a predominant number of defined benefit plans to a predominant number of defined contribution plans, as smaller private sector employers have begun establishing primary pension coverage and larger private sector employers have instituted supplemental pension coverage utilizing defined contribution plans. It found that larger private sector employers and public sector employers have continued to utilize defined benefit plans, while smaller private sector employers have been increasingly utilizing defined contribution plans if pension coverage is provided at all. Employer goals, employer capabilities, and employer perceptions govern the choice of pension plan type. If employment mix and other factors are not controlled for, the public sector provides more generous compensation and benefits than the private sector, but when employment mix and other factors are controlled for, relative generosity is less clear.

In reviewing the results of a comparison of 47 Minnesota retirement arrangements, from a largely self-selected and non-scientific sampling, the Legislative Commission on Pensions and Retirement found that the Minnesota pension practice appears largely to replicate the identified national trends.

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Table 1: Comparison Of Calculated Hypothetical Retiree Retirement Benefit Amounts

Plan	Occupation Type	No. Employees	Retire Age	Service Length	Final Annual Salary	Defined Benefit Plan Benefit	IRC 401(k) Benefit	Other Defined Cont. Plan Benefit	Thrift Plan Benefit	Profit Sharing Benefit
Plan A	Cler/Mgr-Super	Over 1,000	64	30	$48,338	19680	0	0	2400	0
Plan AA	Mgr-Super	Under 25	65	20	$21,132	14076.36				
Plan B	Cler/Mgr-Supv	Over 1,000	63	14	$24,738	4710				
Plan BB	Mgr-Super	Under 25	64	23	$160,000	112668				
Plan C	Clerical	Over 1,000	65	15	$36,000		11340	0	0	0
Plan CC	Mgr-Supr	Over 1,000	65	15	$65,004	12630				
Plan D	Clerical	Under 25	64	23	$35,880	30133.44				
Plan DD	Mgr-Supr	Over 1.000	65	30	$65,004	25260				
Plan E	Clerical	Over 1,000	65	30	$30,000	9820				
Plan EE	Other	Over 1,000	65	20	$50,000	5755	8146			3491
Plan F	Clerical	Under 25	62	16	$25,000	6629.52				
Plan FF	Other	Over 1,000	65	30	$120,000	22389	29081			12464
Plan G	Clerical	Over 1,000	62	12	$26,749	5292				
Plan GG	Other	Over 1,000	65	15	$60,000		18900	0	0	0
Plan H	Clerical	Over 1,000	65	15	$30,000	6750				
Plan HH	Other	Over 1,000	65	10	$30,000	1533	1993			854
Plan I	Clerical	Over 1,000	51	30	$40,951	14328				
Plan II	Prod/Other	Over 1,000	50	30	$60,600	21139.68				
Plan J	Clerical	Over 1.000	65	30	$30,000	13500				
Plan JJ	Production	Over 1,000	65	30	$40,000	13649				
Plan K	Clerical	Over 1,000	62	15	$31,000	4650				
Plan KK	Production	Over 1,000	62	38	$39,083	23256				
Plan L	Executive	101-1000	65	25	$93,600	20985				
Plan LL	Production	Over 1.000	65	15		7920				
Plan M	Executive	101-1000	65	25	$93,600	26318	23897	11949		
Plan MM	Production	Over 1,000	62	20	$58,500	13278.24				
Plan N	Executive	101-1000	65	25	$93,600		23897	11949		19915
Plan NN	Production	Over 1,000	65	30		15840				
Plan O	Mgmt	101-1000	65	25	$41,600	9326				
Plan OO	Retail	Over 1,000	65	5						
Plan P	Mgmt	101-1000	65	25	$41,600	8685	10621	5311		
Plan PP	Staff	100-1000	65	25	$22,880		5842	2921		4868
Plan Q	Mgmt	101-1000	65	25	$41,600		10621	5311		8851
Plan QQ	Staff	101-1000	65	25	$22,880	4160	5842	2921		
Plan R	Mgr-Super	Over 1,000	49	31	$57,970	17032.8				
Plan RR	Staff	101-1,000	65	25	$22,880	5130				
Plan S	Mgr-Super	Over 1,000	62	17	$51,408	13512				
Plan SS	Staff	101-1000	65	25	$22,800	5130				
Plan T	Mgr-Super	Over 1,000	62	18	$87,000	19132.44				
Plan TT	Union	101-1,000	63	22		8284.8				
Plan U	Mgr-Super	Under 25	62	29	$160,000	45689.4				
Plan UU	Union	26-100	65	9		2208				
Plan V	Mgr-Super	Over 1,000	65	30	$60,000	23200				
Plan VV	Union	26-100	65	45		12475.2				
Plan W	Mgr-Super	Under 25	62	19	$126,607	76000.08				
Plan X	Mgr-Super	26-100	65	40	$151,292	53584.56				
Plan Y	Mgr-Super	Over 1,000	65	15	$48,000		15120	0	0	0
Plan Z	Mgr-Super	Under 25	57	14	$108,966	52303.56				

Table 2: Comparison Of Calculated Hypothetical Retiree Member And Employer Contribution Amounts

Plan	Occupation Type	No. Employees	Retire Age	Service Length	Final Annual Salary	Defined Benefit Memb. Contrib.	IRC 401(k) Memb. Contrib.	Other Def. Contr. Employee Contrib.	Thrift Plan Member Contrib.	Def. Benefit Employer Contrib.	IRC 401(k) Employer Contrib.	Other Def. Contr. Employer. Contrib.	Thrift Plan Employer Contrib.
Plan A	Cler/Mgr-Super	Over 1,000	64	30	$48,338	1934	0	0	1000	1934	0	0	1000
Plan AA	Mgr-Super	Under 25	65	20	$21,132								
Plan B	Cler/Mgr-Supv	Over 1,000	63	14	$24,738	1281				1281	0		
Plan BB	Mgr-Super	Under 25	64	23	$160,000					108022			
Plan C	Clerical	Over 1,000	65	15	$36,000	0	3600	0	0	0	1440	0	0
Plan CC	Mgr-Supr	Over 1,000	65	15	$65,004								
Plan D	Clerical	Under 25	64	23	$35,880					108022		3588	
Plan DD	Mgr-Supr	Over 1.000	65	30	$65,004								
Plan E	Clerical	Over 1,000	65	30	$30,000		1500				750		
Plan EE	Other	Over 1,000	65	20	$50,000	0	1500	0	0		2000	1500	
Plan F	Clerical	Under 25	62	16	$25,000					47171			
Plan FF	Other	Over 1,000	65	30	$120,000	0	3000	0	0		4000	3000	
Plan G	Clerical	Over 1,000	62	12	$26,749								
Plan GG	Other	Over 1,000	65	15	$60,000	0	6000	0	0	0	2400	0	0
Plan H	Clerical	Over 1,000	65	15	$30,000								
Plan HH	Other	Over 1,000	65	10	$30,000	0	900	0	0		1200	900	
Plan I	Clerical	Over 1,000	51	30	$40,951								
Plan II	Prod/Other	Over 1,000	50	30	$60,600								
Plan J	Clerical	Over 1.000	65	30	$30,000								
Plan JJ	Production	Over 1,000	65	30	$40,000		2000				1000		
Plan K	Clerical	Over 1,000	62	15	$31,000		3500				700		
Plan KK	Production	Over 1,000	62	38	$39,083								
Plan L	Executive	101-1000	65	25	$93,600					3594.24			
Plan LL	Production	Over 1.000	65	15									
Plan M	Executive	101-1000	65	25	$93,600		5616			1890.72		2808	
Plan MM	Production	Over 1,000	62	20	$58,500		7500				1500		
Plan N	Executive	101-1000	65	25	$93,600		5616					2808	
Plan NN	Production	Over 1,000	65	30									
Plan O	Mgmt	101-1000	65	25	$41,600					1597.44			
Plan OO	Retail	Over 1,000	65	5			Up to 20% salary				40% of first 5% of salary		
Plan P	Mgmt	101-1000	65	25	$41,600		2496			840.32		1248	
Plan PP	Staff	100-1000	65	25	$22,880		1373					686	
Plan Q	Mgmt	101-1000	65	25	$41,600		2496					1248	
Plan QQ	Staff	101-1000	65	25	$22,880		1373			462.18		686	
Plan R	Mgr-Super	Over 1,000	49	31	$57,970								
Plan RR	Staff	101-1,000	65	25	$22,880						878.59		
Plan S	Mgr-Super	Over 1,000	62	17	$51,408								
Plan SS	Staff	101-1000	65	25	$22,800					878.59			

Plan	Occupation Type	No. Employees	Retire Age	Service Length	Final Annual Salary	Defined Benefit Memb. Contrib.	IRC 401(k) Memb. Contrib.	Other Def. Contr. Employee Contrib.	Thrift Plan Member Contrib.	Def. Benefit Employer Contrib.	IRC 401(k) Employer Contrib.	Other Def. Contr. Employer. Contrib.	Thrift Plan Employer Contrib.
Plan T	Mgr-Super	Over 1,000	62	18	$87,000		10000				2000		
Plan TT	Union	101-1,000	63	22						100000			
Plan U	Mgr-Super	Under 25	62	29	$160,000					47171			
Plan UU	Union	26-100	65	9									
Plan V	Mgr-Super	Over 1,000	65	30	$60,000		3000				1500		
Plan VV	Union	26-100	65	45									
Plan W	Mgr-Super	Under 25	62	19	$126,607					39313			
Plan X	Mgr-Super	26-100	65	40	$151,292								
Plan Y	Mgr-Super	Over 1,000	65	15	$48,000	0	4800	0	0	0	1920	0	0
Plan Z	Mgr-Super	Under 25	57	14	$108,966					40938			

Table 3: Comparison Of Other Pension Practices For Calculated Hypothetical Retirees

Plan	Occupation Type	No. Employees	Post-Retirement Adjustments	Other Plan Service Recognition	Early Retirement Incentive	Administrative Expense Source	Subsidized Post-Retirement Medical Insurance	Pre-Retirement Counseling
Plan A	Cler/Mgr-Super	Over 1,000	Automatic	Yes	Periodically	Combination	No	Yes
Plan AA	Mgr-Super	Under 25	No	No	Never	Employer	No	No
Plan B	Cler/Mgr-Supv	Over 1,000	Automatic	Yes	Periodically	Combination	No	Yes
Plan BB	Mgr-Super	Under 25	No	No	Never	Employer	No	No
Plan C	Clerical	Over 1,000	No	No	Infrequently	Combination	No	No
Plan CC	Mgr-Supr	Over 1,000	Ad hoc	No	Infrequently	Plan Trust	Yes	Yes
Plan D	Clerical	Under 25	No	No	Never	Employer	No	No
Plan DD	Mgr-Supr	Over 1.000	Ad hoc	No	Infrequently	Plan Trust	Yes	Yes
Plan E	Clerical	Over 1,000	No	No	Never	Employer	No	No
Plan EE	Other	Over 1,000	No	Yes	Infrequently	Employer	Yes	Yes
Plan F	Clerical	Under 25	No	No	Never	Employer	No	No
Plan FF	Other	Over 1,000	No	Yes	Infrequently	Employer	Yes	Yes
Plan G	Clerical	Over 1,000	No	No	Infrequently	Combination	No	No
Plan GG	Other	Over 1,000	No	No	Infrequently	Combination	No	No
Plan H	Clerical	Over 1,000	Ad hoc	No	Infrequently	Plan Trust	Yes	Yes
Plan HH	Other	Over 1,000	No	Yes	Infrequently	Employer	Yes	Yes
Plan I	Clerical	Over 1,000		No	Infrequently	Employer	Yes	No
Plan II	Prod/Other	Over 1,000		No	Infrequently	Employer	Yes	No
Plan J	Clerical	Over 1.000	Ad hoc	No	Infrequently	Plan Trust	Yes	Yes
Plan JJ	Production	Over 1,000	No	No	Never	Employer	No	No
Plan K	Clerical	Over 1,000	Ad hoc	Yes	Infrequently	Employer	Yes	No
Plan KK	Production	Over 1,000	No	No	Infrequently	Combination	Yes	No
Plan L	Executive	101-1000	Ad hoc	Yes		Employer	No	No
Plan LL	Production	Over 1.000	Ad hoc	No	Infrequently	Plan Trust	Yes	Yes
Plan M	Executive	101-1000	Ad hoc	Yes	Infrequently	Employer	No	No
Plan MM	Production	Over 1,000	Ad hoc	Yes	Infrequently	Employer	Yes	No
Plan N	Executive	101-1000	No	Yes		Employee	No	No
Plan NN	Production	Over 1,000	Ad hoc	No	Infrequently	Plan Trust	Yes	Yes
Plan O	Mgmt	101-1000	Ad hoc	Yes		Employer	No	No
Plan OO	Retail	Over 1,000	No	No	Never	Employer	No	No
Plan P	Mgmt	101-1000	Ad hoc	Yes	Infrequently	Employer	No	No
Plan PP	Staff	100-1000	No	Yes		Employee	No	No
Plan Q	Mgmt	101-1000	No	Yes		Employee	No	No
Plan QQ	Staff	101-1000	Ad hoc	Yes	Infrequently	Employer	No	No
Plan R	Mgr-Super	Over 1,000		No	Infrequently	Employer	Yes	No
Plan RR	Staff	101-1,000	Ad hoc					
Plan S	Mgr-Super	Over 1,000	No	No	Infrequently	Combination	No	No
Plan SS	Staff	101-1000	Ad hoc	Yes		Employer	No	No
Plan T	Mgr-Super	Over 1,000	Ad hoc	Yes	Infrequently	Employer	Yes	No
Plan TT	Union	101-1,000	Ad hoc	No	Never	Employer	No	No
Plan U	Mgr-Super	Under 25	No	No	Never	Employer	No	No
Plan UU	Union	26-100	No	No	Never	Employer	No	No
Plan V	Mgr-Super	Over 1,000	No	No	Never	Employer	No	No
Plan VV	Union	26-100	No	No	Never	Employer	No	No
Plan W	Mgr-Super	Under 25	No	No	Never	Employer	No	No
Plan X	Mgr-Super	26-100	No	No	Never	Employer	No	No
Plan Y	Mgr-Super	Over 1,000	No	No	Infrequently	Combination	No	No
Plan Z	Mgr-Super	Under 25	No	No	Never	Employer	No	No