

July 29, 1999  
Room 5 State Office Building

7th Meeting



LEGISLATIVE COMMISSION ON PENSIONS AND RETIREMENT

MINUTES

Representative Harry Mares called the meeting to order at 10:10 A.M. He noted that the Commission did not yet have a quorum.

**Commission members present at this meeting:**

Representatives Philip Krinkie, Harry Mares, Mary Murphy, Steve Smith and Stephen Wenzel  
Senators Don Betzold, Dean Johnson, Lawrence Pogemiller, LeRoy Stumpf, and Roy Terwilliger

**Agenda Items Discussed**

1. **Approval of Minutes of the Commission Meetings of June 22, 1999**  
Sen. Betzold moved approval of the meeting minutes for the June 22, 1999, meeting. **MOTION PREVAILED.**

4. **Commission Interim Topic: Review of TRA Improved Money Purchase Program Savings Provision (First Consideration)**  
Rep. Mares asked Lawrence A. Martin, LCPR Executive Director, to review the staff memo. Mr. Martin briefly reviewed the differences between a defined benefit plan and a defined contribution plan and noted that MSRS and PERA are defined benefit plans while, at that time, TRA and its predecessors were defined contribution plans. He then reviewed the background and history of the Improved Money Purchase program.

Mr. Martin referred members to the table on page 6 of the memo which showed the number of TRA members involved in each of the TRA programs from 1970 to 1975 and how the number of members shifted over time. He noted that since the Improved Money Purchase Program was never anticipated to produce a higher benefit than the High-five benefit, the IMP savings clause has not been included in the actuarial valuation calculation process. He stated that actuarial information calculated by TRA's actuary is attached to the memo. Their calculations show a range of costs depending on the utilization of the IMP program and the additional costs if the program is expanded to currently ineligible TRA members.

Rep. Mares requested that the record show that attorney David K. Hackley sent a letter to the Commission in opposition to expanding the savings clause eligibility. A copy has been included in members' packets and will be included in the record of this meeting.

Rep. Wenzel asked Mr. Martin to expand and explain his comment that for whatever reason the IMP savings clause was never repealed? Mr. Martin responded that when a savings clause is implemented, it usually has a narrow window to accommodate members who are very near retirement to assure that they are not inadvertently harmed. Savings clauses normally are implemented for a relatively short time period and have a sunset date when it is presumed they are no longer relevant. It is somewhat rare to have a savings clause continue for 20 or 30 years.

Sen. Betzold asked if the IMP savings clause could have been sunsetted without impacting member's rights. Mr. Martin stated that whenever a change is made an argument can be made that it may have impacted someone's rights.

Sen. Johnson asked if passage of Senator Larson's bill would negatively impact TRA. Mr. Martin stated that the IMP savings clause will have a negative impact on TRA ranging from an estimate of a few hundred million dollars up to several hundred million with the members it currently applies to. If the bill passed, it would result in an additional negative impact on TRA. He stated that the TRA funding surplus could be eliminated by the current IMP savings clause eligible members. He also noted that if the stock market made a major correction in the near future, the IMP savings clause would no longer be an attractive option.

Rep. Murphy asked whether the basic premise of any retirement choice was that it be equitable with other choices. Mr. Martin stated that in 1969 TRA had three benefit plans, a career average salary plan, the IMP program (bond investments), and the Variable program (stock investments) all of

program and H.F. 2285 and S.F. 2239.

Marv Hartung, a retired teacher, testified that he taught for forty years, was the oldest and taught the longest of the 14 other teachers who retired with him, and ten of those 14 were in the IMP program and receive a much larger benefit than he does. He testified in support of H.F. 2285 and S.F. 2239 to provide equity.

Mr. O'Neill and Senator Larson made a few closing comments.

Rep. Murphy asked Mr. O'Neill, as an author of the original bill, what the intent of the Legislature was in establishing the high-five program without a sunset on the IMP program.

Mr. O'Neill testified that at that time, the Commission's main concern was the poor funding levels of the State's pension plans and the fact that PERA and MSRS had defined benefit programs while TRA had a "horrible" defined contribution program. The Legislature changed TRA to a defined benefit program, improved all three statewide plans defined benefit programs by changing to a High-five formula, and increased contributions to improve funding over a ten year period. Discussion continued with regard to the Commission and Legislature's actions in dealing with pension issues during this time.

Sen. Stumpf noted that the 1989 legislation that abolished the variable annuity program and allowed all teachers to have the high-five program passed because of the efforts of TRA, MSRS, and PERA and had their full support.

Gary Austin, TRA Executive Director, provided a handout and referred members to the election form provided to teachers in the 1969-1972 time period. He noted the box in the center of the form in bold capital letters which directed teachers not to complete the form unless they wished to change from the Improved Money Purchase program to a different program. Teachers currently included in the program are teachers who did not submit the form either by choice or by default. In 1973, the career-average formula changed to the high-five formula and was a major benefit improvement that more than doubled benefits and the savings clause was added. In 1974, there was great pressure to allow variable annuity participants access to the high-five formula program, legislation was passed to permit that and resulted in TRA having only two programs. In 1978, there was again great pressure on the part of teachers to have future service covered only by the high-five formula and legislation passed to provide that. In 1989, TRA incurred an \$120 million actuarial loss in response to great pressure from teachers to eliminate the variable annuity fund and permit all service credit to be calculated under the high-five formula. Mr. Austin reviewed the interest rates used in the IMP program calculation. He then reviewed a table comparing the high-five benefit with the IMP benefit. He noted that the IMP program only exceeded the high-five benefit in the last three years. Mr. Austin reviewed the number of teachers that retired under the IMP program since 1997. He testified that in 1998, TRA began a review of their files to identify which teachers were eligible for the IMP program and in 1999 sent letters to approximately 3,300 eligible teachers with benefit comparison estimates. He also reviewed the demographic data on those teachers and the Buck Consultant's estimated cost of the IMP program.

Sen. Betzold asked why the savings clause provision wasn't sunsetted? Mr. Austin testified that this was an obscure rarely used provision until 1997. When it began having more of an impact in 1997, it was too late since it may have been construed to be a benefit takeaway. Sen. Betzold asked why legislation wasn't sought to have members eligible for the savings clause elect between the coverages and then sunset the savings clause provision instead of having members wait until their retirement to elect a benefit? Mr. Austin testified that there were many ways of dealing with this issue. Sen. Betzold asked why the Legislature wasn't informed that TRA was sending out these letters and of the potential uproar that might cause. Mr. Austin testified that he had sent a letter to Commission staff advising that TRA was going to send letters to IMP eligible members.

Sen. Stumpf asked why TRA didn't sunset the IMP savings clause when the variable annuity program was terminated in 1989? Mr. Austin testified that the IMP savings clause was not an issue in 1989 because of the large disparity between the benefits that the IMP savings clause would have provided and the high-five formula benefit. Sen. Stumpf stated that TRA must have had some idea that the IMP savings clause could have an impact at some point in time. Mr. Austin testified that a lot has happened since 1989. Further comments and discussion followed.

Rep. Murphy asked whether any TRA Board members were at this meeting? Mr. Austin testified that there were TRA Board members present. Rep. Murphy asked if the TRA Board had held a hearing on this issue? Mr. Austin testified that the TRA Board had a hearing on this issue and the

TRA Board took the position that the IMP savings clause should not be expanded beyond the current eligible teachers without adequate funding to support that action. He testified that if the IMP savings clause was expanded to include the group represented by Mr. O'Neill additional groups would seek the benefit.

Sen. Johnson asked whether all of the benefit options were discussed and provided in writing at pre-retirement counseling sessions before the 1989 legislation? Mr. Austin testified that he does not know what exactly might have been provided then since he was not TRA's Director at that time. He testified that prior to 1989, teachers pressured for several years to eliminate the variable annuity because members retiring under that program were receiving a significantly smaller benefit than members retiring under the high-five formula.

Rep. Mares asked whether TRA drafted or recommended the IMP savings clause? Mr. Austin testified that he would research that issue.

Hank Stankiewicz, representative of Education Minnesota, provided a handout and testified in opposition to H.F. 2285 and S.F. 2239. He testified that Education Minnesota considered a motion to expand the IMP program to teachers from the 1968-1969 school year who elected not to stay in the IMP program and the motion was overwhelmingly defeated. He testified that the motion was defeated because delegates knew TRA members freely filed their election forms during the 1969-1972 time period, that the cost of expanding the program would exceed the new money appropriated for K-12 education this school year, and that no teacher has lost any benefits. He testified that benefits have improved substantially since 1969. The TRA surplus should be used to benefit all teachers. In noting inequities he mentioned that post-1989 hirees have an age 66 normal retirement age and no Rule of 90 option although their contribution is the same as teachers eligible for different benefits. Some members have taken advantage of windfalls like the teachers who retired as soon as the TRA accrual rate became 1.63 and did not have to pay the contribution increase necessary to fund that higher accrual rate. The Education Minnesota attorneys have not found any legal inequities or rights violations to date. Mr. Stankiewicz stated that one of Education Minnesota's biggest victories in 1989 was finally getting the variable annuity program eliminated in response to pleas from teacher's all over the State at a cost to TRA of \$130 million.

Rep. Mares asked whether Education Minnesota played a role in informing members during the 1969-1972 election period? Mr. Stankiewicz responded that he would check into that matter.

Mary Budde, a teacher since 1966, requested an opportunity to testify since her situation wasn't addressed by previous testimony. She testified that in 1972 she completed her form and selected the combined money purchase program which was 4/7's IMP because it allowed retirement at age 55. She selected an IMP program but is not eligible for the savings clause. She testified in support of expanding the eligibility and remembering the members who selected the 4/7's IMP combination in future discussion of this issue.

Rep. Mares recessed the Commission for five minutes to allow the room to clear at the conclusion of testimony on this topic.

### **3. Commission Consideration of Proposed Actuarial Assumption Changes**

#### **- Thomas K. Custis, F.S.A., Milliman & Robertson, Inc.**

Mr. Thomas Custis, Commission actuary from Milliman & Robertson, Inc., provided a handout and began his presentation on recommended actuarial assumption changes. To inform members as to why assumptions are so important, he reviewed an equation that read "benefits plus expenses equal contributions plus interest." That means that over time all expenditures are funded either by contributions or interest and the determination of benefits defines how much the required contributions need to be. Mr. Custis stated that actuarial assumptions help a fund reach its target. He noted that every four years an experience study is performed for the three statewide funds which help determine the appropriate actuarial assumptions for each of the plans. The last experience studies were completed in 1997 for the July 1, 1992 to June 30, 1996 period. Milliman & Robertson, Inc. developed a set of recommended actuarial assumption changes based on those experience studies and the assumption changes have been reviewed, adjusted, and accepted by the fund directors and consulting actuaries for the funds. The recommendations include updating mortality assumptions, age related retirement assumptions, select normal withdrawal service assumptions, and combined service annuity assumptions.

Sen. Pogemiller asked what modifying the merit and longevity component of salary scales meant? Mr. Custis responded that it referred to base salary increases and promotional salary increases. Sen. Pogemiller stated that the change increased the difference between younger shorter service and

older longer service members and questioned what actual experience indicated the necessity for that change. Mr. Custis responded that salaries moved up faster during younger, shorter service than previously was assumed and that longevity and merit increases were not as frequent as previously assumed.

Mr. Custis referred members to the required funding table that showed changes in the mortality table assumptions would increase significantly the required cost of the plans while changing the salary increase assumptions would slightly decrease the required cost for PERA and MSRS. Changes in the disability assumptions would provide a slight decrease for all three funds. Changes in retirement age assumptions would increase PERA costs, decrease MSRS costs, and have minimal impact on TRA costs. Changes in withdrawal assumptions would significantly impact PERA, slightly impact MSRS, and minimally impact TRA. Changes in the combined service annuity assumptions would impact all three funds and significantly impact PERA. He then referred members to the funding ratio table which showed what impact changing these assumption rates would have on the actuarial accrued liability of the three funds. He noted that the impact on TRA would be to slightly decrease its funding ratio, on MSRS it would improve the funding ratio, and PERA would have a significant decrease in its funding ratio. Mr. Custis noted that TRA's contribution requirements would show a sufficiency, MSRS's contribution requirements would show a slight deficiency, but for PERA the increase in normal cost and increase in the unfunded liability would have a major impact on the contribution deficiency measure. He then reviewed the results of changing the actuarial assumptions for the three major plans if used on their 1998 valuations. He noted that the final column on the results pages showed the results of both changing the actuarial assumptions as well as adopting his two recommended changes in actuarial methods (one would change the method of valuing assets and the other would recognize the negative unfunded on a 30 year basis). Implementing both changes would increase the sufficiency for TRA and MSRS but would cause a significant deficiency for PERA. Mr. Custis noted that the biggest factor causing PERA's deficiency, according to PERA's actuary, seems to be attributable to the change in withdrawal assumptions. Milliman's numbers validate that conclusion for the most part as indicated in the third column's increase in deficiency compared to the second column's deficiency where the withdrawal assumption change was not used. He then reviewed PERA's turnover activity which showed that employees with less than one year of service turnover at a rate twice as fast as the current assumption but withdrawal assumption rates are too high for employees with one to three years of service. Using the higher decrements, regardless of service, gives an understatement of costs and greatly impacts PERA but doesn't have as great a negative impact on MSRS and TRA because they have a larger number of short service employees who remain in service.

Rep. Mares asked if the problem with PERA was known previously? Mr. Custis responded that he had recommended a withdrawal assumption change after completing the first set of experience studies six years ago. PERA's actuary at that time felt that in total, the turnover rate seemed fairly close and the refinement in withdrawal assumptions was unnecessary. Rep. Mares asked what the deficit amount for PERA would be and what increase would be required in the employer and employee contribution rate? Mr. Custis responded that PERA would have a 2.2% deficiency and that would require a 1.1% increase in both employee and employer contributions. He stated that the past year's investment gains may mitigate the deficiency somewhat but corrective action will still be necessary.

Rep. Krinkie asked whether the IMP provision was taken into account when measuring the impact of the assumption changes on TRA? Mr. Custis responded that the numbers do not reflect IMP eligible members since he did not have that data when the 1998 TRA valuation was completed.

Mr. Martin stated that most of the recommended actuarial assumption changes are administrative and could be passed by the Commission immediately but economic assumption changes, such as the recommended salary assumption change, require legislation and would have to wait until the next Legislative Session. He asked Mr. Custis what he would advise: should the administrative assumptions be done for the new set of actuarial valuations; or should the Commission wait until next Session and do them all at once. Mr. Custis advised changing all of the assumptions at once because of the different impact each change has on the funding status of the plans. However, if legislative changes were recommended during the next session, he would prefer to use the new assumptions when costing out those potential changes. Based on that information, Mr. Martin recommended waiting until early February to make the actuarial assumption changes and he will prepare the necessary legislation to change the economic assumptions and the motion to change the administrative assumptions.

5. **Mandated Commission Interim Project: Appropriate Means For Partially Employer-funded Tax-sheltered Savings Opportunities For Educational Employees (First Consideration)**

Mr. Martin reviewed the staff memo prepared by Edward Burek, LCPR Deputy Director, who was unable to present due to a family emergency out of town.

Mr. Martin stated that this was a mandated study required by the omnibus pension bill. He noted that this issue dealt with retirement savings separate from the State's normal pension plans. The State has two programs in statute that permit employer matching contributions, the 457 Deferred Compensation Program (open to all employees) and the 403(b) Tax Sheltered Annuity Program (open only to educational employees). He referred members to the comparison of the two plans on page 2 of the memo. He noted that the Commission was directed to consider a single provider for 403(b) programs, as recommended by the State Board of Investment's 1997 report, as well as to consider allowing the program to continue with an unrestricted number of vendors. Previous law permitted ten vendors access to this program and SBI had approved eight. The 1999 law increased the number of vendors permitted to 25, 20 insurance companies and five mutual fund companies. This study will give the Commission an opportunity to determine the best way to implement employer and employee contributions to 403(b) plans. The staff memo provided Commission members with background information on how these tax-sheltered annuity plans have evolved to this point. The next memo on this topic will deal with the SBI recommendation to have a single provider. The final memo will deal with the unrestricted number of vendors issue.

6. **Mandated Commission Interim Project: Comparability of Public Sector and Private Sector Employee Pension and Other Post Retirement Benefits (First Consideration)**

Mr. Martin began to review the staff memo and stated that he is looking for direction from the Commission on this topic.

Rep. Krinkie stated that the mandated study language originated in the House State Government Finance Division Committee. He recommended that the Commission select one of the four options provided in the staff memo as the basis for the study. Discussion followed.

Mr. Martin referred members to page three of the staff memo and began to review the four options that he had identified. The first option would require staff to assemble public and private benefit comparisons and prepare a report. The second option would require staff to compare two public pension plans' benefit provisions with ten to 20 private plans' benefit provisions. The third option would require staff to calculate hypothetical benefits for certain sample employees in both the public and private sector. The fourth option would have the Commission actuary calculate the normal cost of public and private pension plans using a selected membership group.

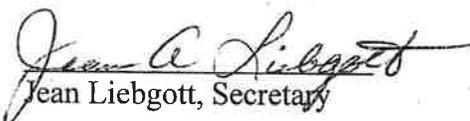
Rep. Krinkie stated that he is interested in learning how public pension benefits compare with private pension benefits.

Sen. Stumpf stated that he thought selecting option one would be beneficial. He also suggested checking with NCSL or CSG to see what information they already have available in comparisons of this sort.

Rep. Krinkie stated that he hoped that staff would assemble NCSL and foundation comparisons but that he hoped the study would go beyond that. Rep. Krinkie moved option three. He then stated that if staff began with option three and it became clear that the scope was too broad or wouldn't fit within the timeframe necessary, staff would have time to confer with the Commission at the next meeting. Rep. Mares suggested selecting option one and three and reexamining the topic at the next meeting. Sen. Betzold suggested sampling a mid-management position and a laborer position similar to a MNDOT employee position.

Rep. Mares announced that the next Commission meeting would be in September.

The meeting adjourned at 1:35 P.M.

  
Jean Liebgott, Secretary

*The sound system malfunctioned the first 20 minutes of the meeting so there is no tape for the beginning of this meeting.*