4Q2009 IAC Meeting Materials

IAC Meeting – February 16, 2010

Statewide Retirement Systems Presentation

Retirement Systems of Minnesota

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Statewide Retirement Systems Funding Updates

Mary Vanek, PERA Executive Director
Dave Bergstrom, MSRS Executive Director
Laurie Hacking, TRA Executive Director

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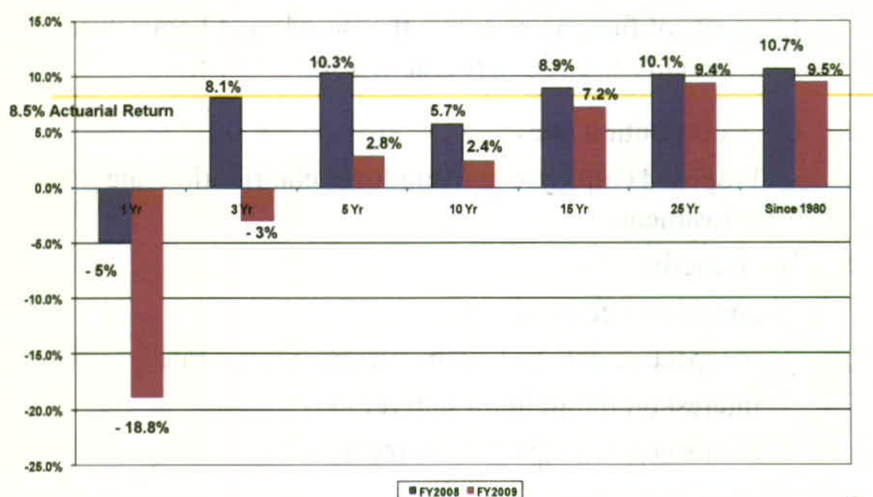
Why Are We Having These Discussions?

Comparison of SBI Average Returns – for periods ending 6/30/2008 and 6/30/2009



Return for FY 2010 to-date: approximately 15%

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Basic Pension Funding Principle

C + I = B + E

Contributions + Investments = Benefits + Expenses

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Common Modifications to Address Funding

Elements of funding principle the Boards and Legislature could modify to address recent investment losses

- C – Contribution rates
  - Proposed employee and employer contribution rate adjustments
- B – Benefits
  - annual retiree increases
  - prospective deferred augmentation interest rate
  - interest on future lump sum refunds
  - interest on re-employed retiree accounts

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Financial Status of PERA General Fund

Fiscal Year 2009	July 1, 2009 Actuarial Value (5 yr smoothing of investment losses)	July 1, 2009 Market Value (no smoothing of investment losses)
Funding Ratio (Assets as % of Liabilities)	69.99 %	53.81 %
Current Contributions*	12.88 % of pay	12.88 % of pay
Contributions Needed	15.55 % of pay	19.61 % of pay
Contribution Deficiency	(2.67) % of pay	(6.73) % of pay

* Employee rate = 6%; Employer rate = 7% (effective 01/01/10)

Source: Mercer Consulting, FY 09 annual actuarial valuation

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Financial Status of PERA P&F Fund

Fiscal Year 2009	July 1, 2009 Actuarial Value (5 yr smoothing of investment losses)	July 1, 2009 Market Value (no smoothing of investment losses)
Funding Ratio (Assets as % of Liabilities)	83.22 %	63.55 %
Current Contributions*	23.50 % of pay	23.50 % of pay
Contributions Needed	29.99 % of pay	39.13 % of pay
Contribution Deficiency	(6.49) % of pay	(15.63) % of pay

*Employee rate = 9.4%; Employer rate = 14.1%

Source: Mercer Consulting, FY 09 annual actuarial valuation

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Financial Status of PERA Correctional Fund

Fiscal Year 2009	July 1, 2009 Actuarial Value (5 yr smoothing of investment losses)	July 1, 2009 Market Value (no smoothing of investment losses)
Funding Ratio (Assets as % of Liabilities)	94.85 %	72.93 %
Current Contributions*	14.58 % of pay	14.58 % of pay
Contributions Needed	14.03 % of pay	16.77 % of pay
Contribution Deficiency	0.55 % of pay	(2.19) % of pay

*Employee rate = 5.83%; Employer rate = 8.75%

Source: Mercer Consulting, FY 09 annual actuarial valuation

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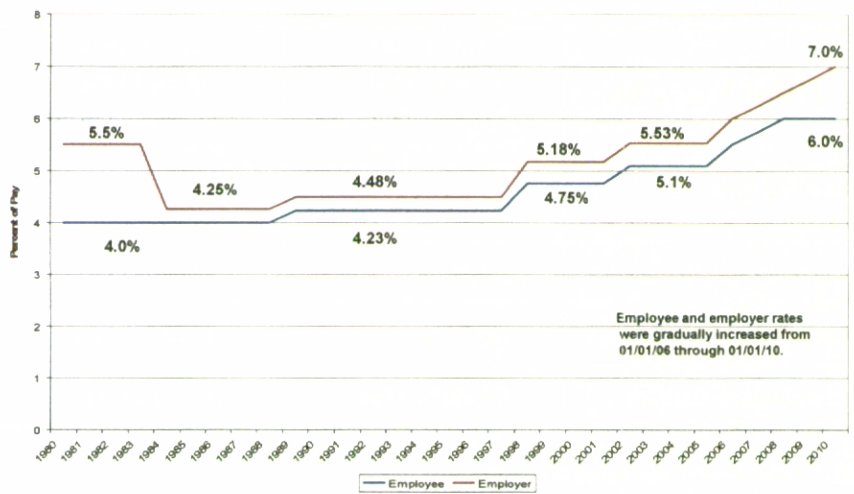
History of PERA General's Contribution Rates



The PERA General Plan's contribution rates have been adjusted several times since the employer additional contribution rate, assuming the plan was adequately funded at 78 percent at the time, was reduced in 1984. Two adjustments thereafter accompanied benefit modifications; more recent rate changes did not.

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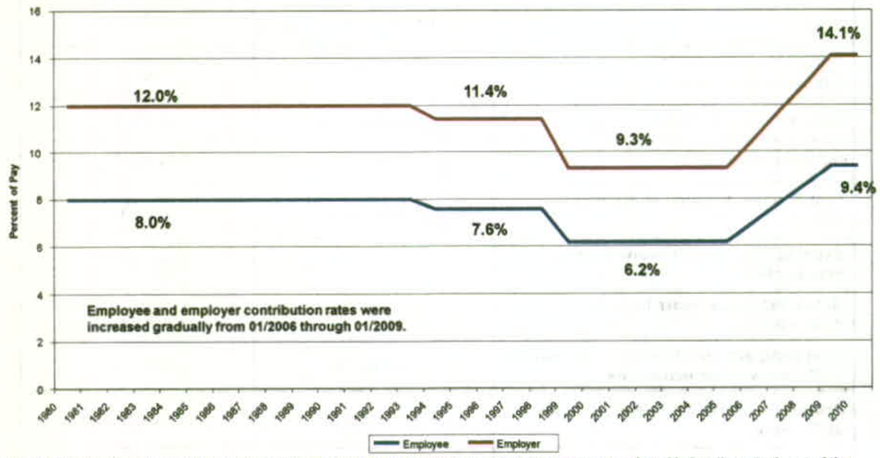
History of Police and Fire Plan's Contribution Rates



Contribution rates were reduced because the plan was over 100 percent funded, but the rates were reduced below the actual cost of the benefits, so when the markets eroded the excess assets and created an unfunded liability the rates had to be significantly increased to bring them back up to the annual cost of the benefits plus additional to pay unfunded portion. 9

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Path to PERA Long-Term Sustainability

Where do we go from here?

- ***Shared responsibility and sacrifice***– active members, employers, deferred members and benefit recipients will need to be part of the solution.
  - ✓ Reduce annual benefit recipient adjustment

    Decrease annual adjustment from 2.5 percent to 1 percent until plans are again at least 90 percent funded (market value).
  - ✓ Increase contributions 0.5 percent

    Coordinated Plan shared equally between employees & employers

    Police & Fire Plan – shared between employees and employers
  - ✓ Reduce certain active and former member benefits
    - Reduce interest rate on refunds from 6 percent to 4 percent
    - Reduce deferred interest for current deferred members and future terminated vested members to 1 percent --currently 3 percent to age 55 and 5 percent thereafter for those hired prior to July 1, 2006 or 2.5 percent for all years for those hired after July 1, 2006.
    - Increase vesting to five years
    - Eliminate interest on re-employed retiree accounts .

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Path to PERA Long-Term Sustainability

What do we save if Board's recommendations are adopted?

	PERA General	PERA P & F
Modify annual increase: 1.0 percent for future yrs. *	3.6 %	9.45 %
Reduce deferred interest	0.45 %	0.45 %
Increase contributions	0.50 %	0.50 %
Cost Change/adoption of assumption changes	(0.40) %	N/A
Expected savings/revenue from proposals	**4.15%**	**10.40%**
***Actuarial* value contribution deficiency**	**(2.67) %**	**(6.49) %**
Resulting *actuarial* value contribution sufficiency after proposals	**1.48 %**	**3.91 %**
Projected *market* value contribution deficiency	**(6.73)%**	**(15.63)%**
Remaining *market* value contribution deficiency after proposals	**(2.58)%**	**(5.23)%**

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* Until plans are 90 percent funded

Source: Mercer Consulting Services

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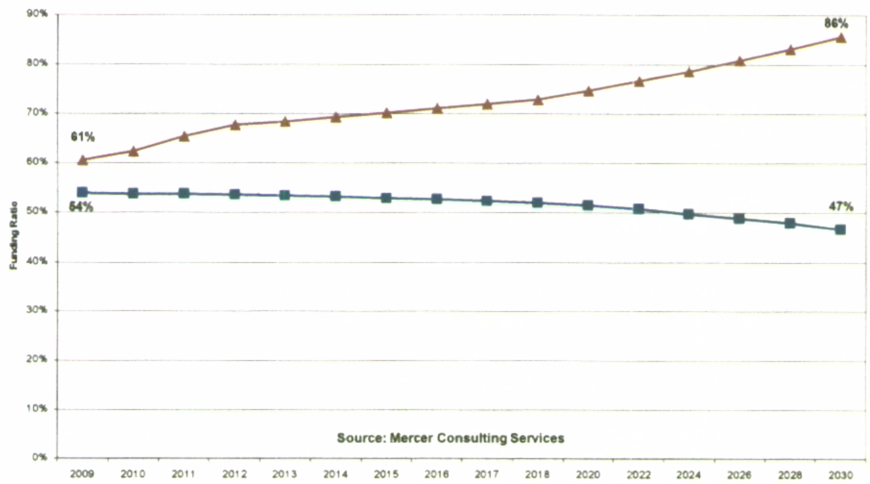
Path to PERA Long-Term Sustainability



Assumes no benefit changes, no contribution increases and 8.5 percent annual return.

Assumes reduction in deficiency of 3.65 percent; contribution increase of 0.5 percent of pay; 11 percent return for three years; 8.5 percent each year thereafter

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Financial Status of MSRS General Plan

Fiscal Year 2009	July 1, 2009 Actuarial Value 30 Year Amortization (5 yr smoothing of investment losses)	July 1, 2009 Market Value 30 Year Amortization (no smoothing of investment losses)
Funding Ratio (Assets as % of Liabilities)	85.9 %	65.61%
Current Contributions	10 % of pay	10 % of pay
Contributions Needed**	11.5 % of pay	16.25 % of pay
Contribution Deficiency**	(1.5) % of pay	(6.25) % of pay

•Source: Mercer Consulting, FY 09 annual actuarial valuation – EE rate = 5%; ER rate = 5% (eff. 07/01/10)

** 2010 Legislation to propose 30 year amortization; amounts estimated using FY09 valuation results

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Financial Status of State Patrol Plan

Fiscal Year 2009	July 1, 2009 Actuarial Value (5 yr smoothing of investment losses)	July 1, 2009 Market Value (no smoothing of investment losses)
Funding Ratio (Assets as % of Liabilities)	80.58 %	62.05 %
Current Contributions	26.0 % of pay	26.0 % of pay
Contributions Needed	38.16 % of pay	50.21 % of pay
Contribution Deficiency	(12.16) % of pay	(24.21) % of pay

* Source: Mercer Consulting, FY 09 annual actuarial valuation - EE rate = 10.4%; ER rate = 15.6%

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Financial Status of MSRS Correctional Fund

Fiscal Year 2009	July 1, 2009 Actuarial Value (5 yr smoothing of investment losses)	July 1, 2009 Market Value (no smoothing of investment losses)
Funding Ratio (Assets as % of Liabilities)	71.88 %	55.62 %
Current Contributions	20.70 % of pay	20.70 % of pay
Contributions Needed	24.85 % of pay	28.57 % of pay
Contribution Deficiency	(4.15) % of pay	(7.87) % of pay

* Source: Mercer Consulting, FY 09 annual actuarial valuation – EE rate = 8.60%; ER rate = 12.10% eff. 7/1/2010

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General Plan Contribution History

2010 Contribution Rates: 5.0% Employee **&** 5.0% Employer **Contribution**

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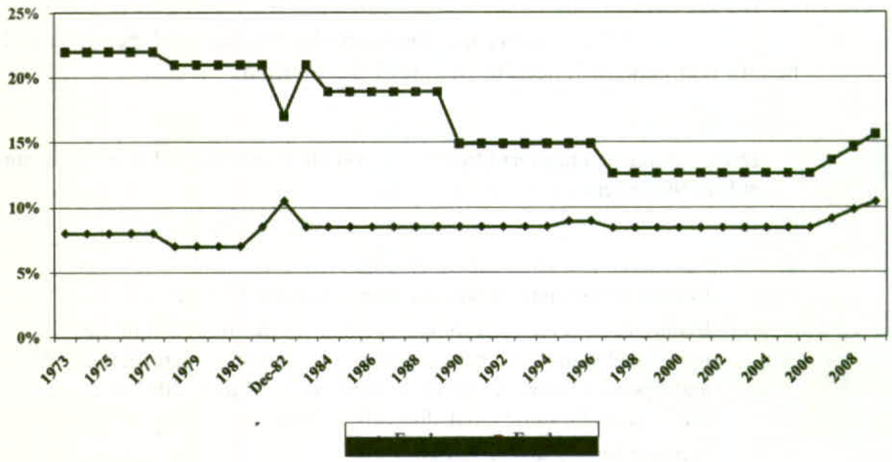
State Patrol Contribution History



2009 Contribution Rates: 10.4% Employee & 15.6% Employer Contribution

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Correctional Plan Contribution History

2010 Contribution Rates: 8.6% Employee & 12.1% Employer

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Path to MSRS Long-Term Sustainability

Where do we go from here?

- *Shared responsibility*– active members, employers, deferred members and benefit recipients will need to be part of the solution.
  - ✓ Reduce annual benefit recipient adjustment

    Decrease annual adjustment from 2.5 percent to 2 percent until plans are again at least 90 percent funded (market value).
  - ✓ Extend amortization to 30 years and modify some actuarial assumptions.
  - ✓ Reduce certain active and former member benefits
    - Reduce interest rate on refunds from 6 percent to 4 percent
    - Reduce deferred interest for current deferred members and future terminated vested members to 2 percent --currently 3 percent to age 55 and 5 percent thereafter for those hired prior to July 1, 2006 or 2.5 percent for all years for those hired after July 1, 2006.
    - Increase vesting to five years
    - Eliminate interest on re-employed retiree accounts .

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Source: Mercer Consulting Services

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Path to MSRS Long-Term Sustainability

Contribution rate impact of the Board's recommendations

Proposals	General	Correctional	State Patrol
Modify annual increase: 2.0 percent for future yrs. *	0.9%	1.7%	4.10%
Reduce deferred interest	0.7%	1.2%	0.20%
Increase contributions	0.0%	0.0%	12.00%
Cost Change/adoption of assumption changes	1.10%	N/A	N/A
Expected savings/revenue from proposals	**2.70%**	**2.9%**	**16.3%**
***Actuarial* value contribution deficiency**	**(1.5) %**	**(4.15) %**	**(12.16) %**
Resulting *actuarial* value contribution sufficiency after proposals	**1.20%**	**(1.25)%****	**4.14%**
Projected *market* value contribution deficiency	**(6.25)%**	**(7.87)%**	**(24.21)%**
Remaining *market* value contribution deficiency after proposals	**(3.55)%**	**(4.97)%**	**(7.91)%**

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* Until 90% funded

**Future savings from longer vesting and benefit reductions

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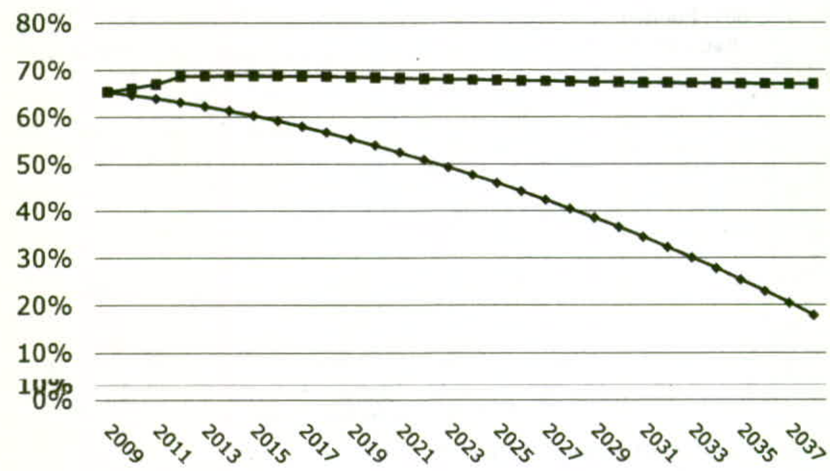
Path to long-term sustainability



*Assumes no benefit changes, contribution changes & 8.5% investment return

*Assume a 3.25% reduction in deficiency & three years of 11% returns;8.5% thereafter

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Financial Status of TRA

Fiscal Year 2009	July 1, 2009 Actuarial Value (5 yr smoothing of investment losses)	July 1, 2009 Market Value (no smoothing of investment losses)
Funding Ratio (Assets as % of Liabilities)	77 %	60 %
Current Contributions	11.69 % of pay	11.69 % of pay
Contributions Needed	16.81 % of pay	22.76 % of pay
Contribution Deficiency	(5.12) % of pay	(11.07) % of pay

* Source: Mercer Consulting, FY 09 valuation – EE rate = 5.5%; ER rate = 5.5%

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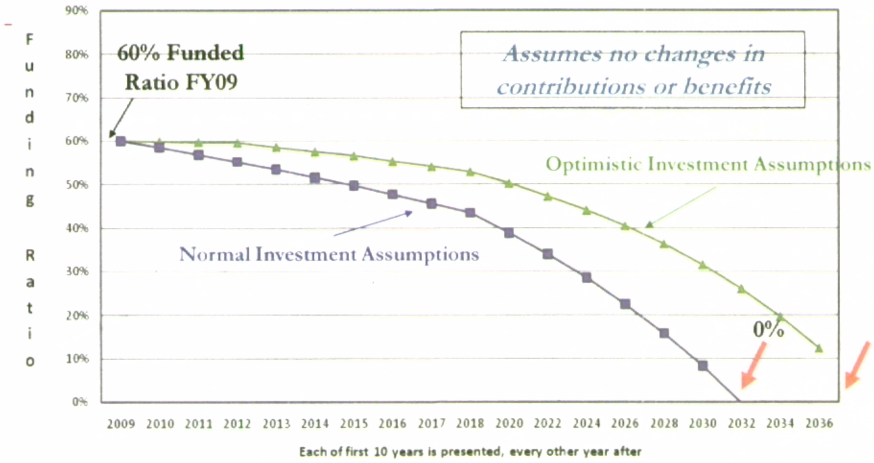
What if we do nothing?



■ Purple Funded %: Current Contributions (11.75%), 8.5% investment return in all years

▲ Green Funded %: Current Contributions (11.75%), 11% investment return for 3 years; 9.5% thereafter

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How did we get here?

1. Severe market downturns in 2000's
   - ✓ Market declines in 2001- 2002 – down 15%+
   - ✓ Market plummets in 2008-2009 – down 24%

2. Extra investment returns of 1990's not retained in TRA Fund –
   - ✓ Large increases in retiree annual increases – 9.7%/year, 1997-2000; 3/4th of current unfunded liability is due to Post Fund; over 60% of TRA liabilities are for retirees
   - ✓ Precipitous rollback in TRA's employER & employEE contributions
     - EmployER rate cut from 8.14% to 5.0%
     - EmployEE rate cut from 6.5% to 5.0%
     - Rate cut = to $176 million/year

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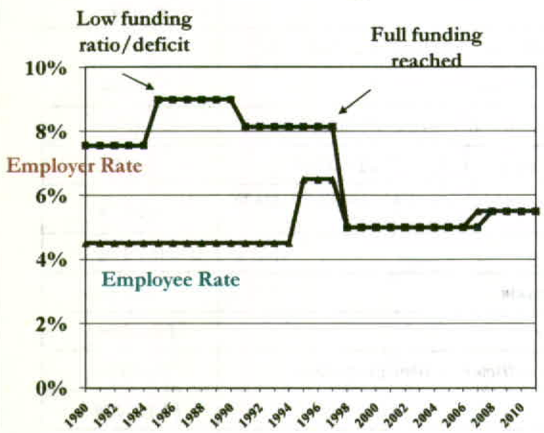
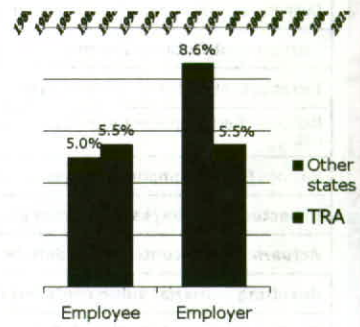
TRA Contributions Higher in Past



Employer /Employee Contributions in Other States



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Path to TRA Long-Term Sustainability

Where do we go from here?

- *Shared sacrifice* – active members, employers, deferred members and benefit recipients will need to be part of the solution.
  - ✓ Reduce annual benefit recipient adjustment
    Temporary 2-year suspension (Jan. 2011 and Jan. 2012)
    2 percent annual increase thereafter until plan is stabilized
  - ✓ Increase employee and employer contributions - phased in over 4 years
    2 percent for employers – phased in 0.5% per year, July 1, 2011 – July 1, 2014
    2 percent for employees – phased in 0.5% per year, July 1, 2011 – July 1, 2014
  - ✓ Reduce certain active and former member benefits
    Reduce interest rate on refunds to 4%; reduce deferred interest for current deferred members and future terminated vested members to 2%; eliminate interest on re-employed retiree accounts.
- *Re-evaluation of all elements in 5 years* – Investment returns will have a major impact (unknown).

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Path to TRA Long-Term Sustainability
TRA Board Recommendations

Proposals	Savings/revenue estimate
Modify annual increase: 2 percent for future years until fund stabilized	2.0%
Suspend annual increase for two years (2011-12)	1.0 %
Increase contributions: 2% employers, phased in 0.5%/yr, 2011-2014	2.0 %
Increase contributions: 2% employees; phased in 0.5%/yr, 2011 - 2014	2.0 %
Reduce deferred interest rate to 2%, reduce refund rate to 4% and ELSA rate to 0%	0.55 %
Savings from assumption changes	0.20 %
Expected revenue/savings from proposals	**7.75 %**
***Actuarial* value contribution deficiency**	**(5.12%)**
Resulting *actuarial* value contribution sufficiency after proposals	**2.63%**
***Market* value contribution deficiency**	**(11.07%)**
Remaining *market* value contribution deficiency after proposals	**(3.32%)**

Source: Mercer Consulting Services

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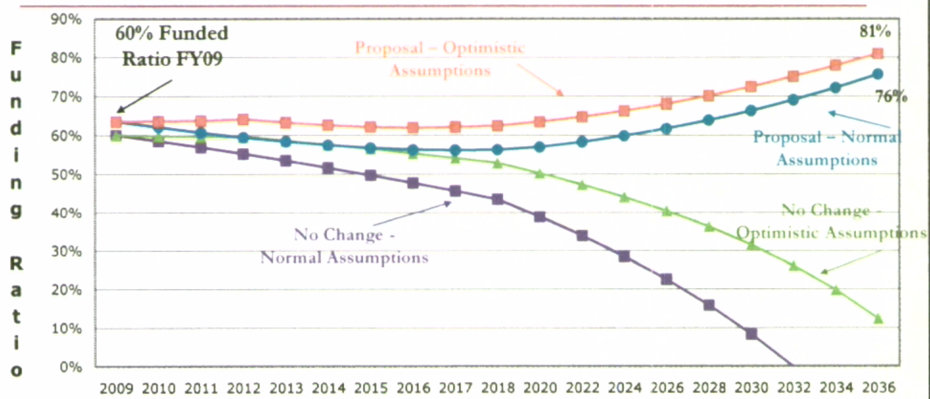
Path to TRA Long-Term Sustainability



Each of first 10 years is presented, every other year after

- **Purple:** Current Contributions (11.69%), no changes in contributions/benefits, 8.5% return in all years
- **Green:** Current Contributions (11.69%), no changes in contributions/benefits, 11% return for 3 yrs; 9.5% thereafter
- **Blue:** Higher Contributions (15.69%), 2 year COLA suspension with 2% thereafter, reset amortization period in 2016, 8.5% return in all yrs
- **Red:** Higher Contributions (15.69%), 2 year COLA suspension with 2% thereafter, reset amortization period in 2016, 11% return for 3 yrs; 8.5% thereafter

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* Source: Mercer Consulting actuarial projections, 12/16/09, 1/22/10

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MN Public Pensions Important to State

- MN's public pension systems serve nearly one-half million persons, 1 in 10 Minnesotans
- More than 90 percent of the systems' benefit recipients reside in Minnesota
- Systems paid out over $2.5 billion in benefits which added $3.3 billion on state economy and led to 22,500 additional jobs statewide
- State/local taxes paid by recipients and holders of new jobs exceeded public employer pension contributions to the systems by $80 million annually
- Economic impact of pension benefits was larger than the gross state product from mining and 92% of agricultural (crop/animal) production.

Source: Lubov, Andrea. "Measuring the Impact of Minnesota's Retirement Systems, March 2008

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What are other states considering?

Actions Taken or Under consideration	State or Local Government
Contributions/Revenues	
Contribution increases	California, Cincinnati, Colorado, Illinois, Iowa, Louisiana, Missouri, Montana, Nebraska, New Hampshire, New Mexico, Ohio, Oklahoma, Oregon, Texas, Utah, Vermont, Virginia, West Virginia, Wisconsin, Wyoming
Contribution cuts/ holiday	New Jersey
Change actuarial techniques	California, Louisiana, Massachusetts, Missouri, Oregon, Vermont, Washington
Pension Obligation Bonds	Illinois, Pennsylvania
Taxes – on pension income	Illinois, Indiana, Philadelphia, Montana
Benefits	
COLA cuts	Colorado, Georgia, Illinois, Louisiana, Massachusetts, Montana, Nevada, New York, Ohio, Rhode Island, South Dakota, Wisconsin, Virginia
Increase normal retirement age or minimum eligibility age, steepen early retirement penalty	California, Cincinnati, Colorado, Kansas, Kentucky, Illinois, Massachusetts, Montana, Nevada, New Mexico, New York, Ohio, Rhode Island, Texas, Vermont, Virginia
Lower benefit tier/ lower formula for future service/new hires	California, Illinois, Nevada, New Mexico, New York, Rhode Island
Switch to DC or hybrid DB/DC	Georgia, Kansas, Louisiana, Massachusetts, Montana, New Jersey, Orange County, Rhode Island, Utah, Virginia
Increase vesting period	Iowa, Massachusetts, New York
Increase high-X salary period	California, Colorado, Iowa, Massachusetts, Montana, Ohio, Rhode Island, Texas
Early retirement incentives to reduce workforce	Connecticut, Iowa, Maine, Vermont

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