Newsletter of the Public Employees Retirement Association of Minnesota mnpera.org

PERA NEWS

Assets Over $25 Billion
Serving over 450,000 public employees in Minnesota

GENERAL | POLICE & FIRE | CORRECTIONAL

SPRING 2018

Spring at Minnehaha Falls in Minneapolis

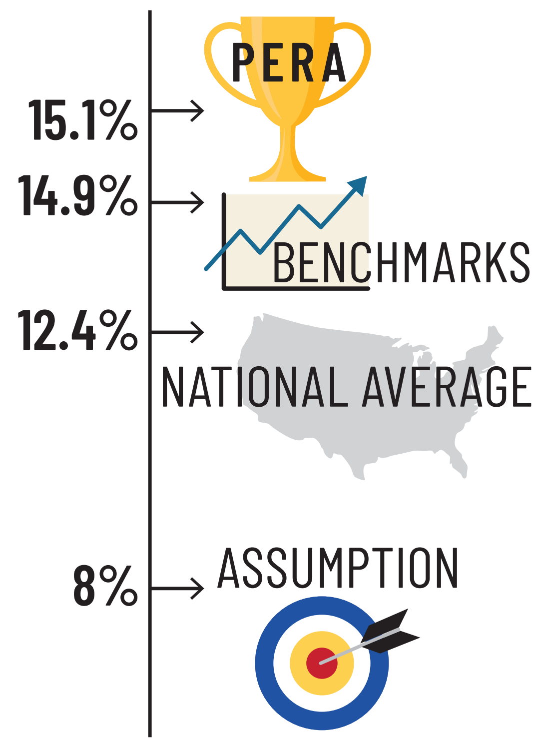
Administer and promote sustainable retirement plans and provide services that our members value.

Strong year for PERA investments

The investment performance for PERA's three largest retirement plans—the General Employees, Police & Fire, and Correctional Plans—for the fiscal year ending June 30, 2017 was excellent. The Combined Fund posted a 15.1 percent rate of return for the 12-month period.

EXCEEDING EXPECTATIONS

The Minnesota State Board of Investment (SBI) invests PERA's financial assets. PERA's assets are pooled with assets of other active members and benefit recipients of Minnestoa State Retirement System (MSRS) and Teachers Retirement Association (TRA) into the Combined Funds. To maximize the long-term rate of return, about 60 percent of assets are invested in domestic and international common stocks. About 20 percent are invested in bonds or fixed income securities and another 20 percent are invested in alternative assets. The diversity of holdings offers the opportunity to enhance returns and reduce the risk and volatility of the total portfolio.



Whether measured against the assumed rate of return, other pension funds nationally, or SBI's benchmarks for each asset class, the 15.1 percent investment return for the fiscal year ending June 30, 2017, was favorable for PERA's pension plans.

WINNING IN THREE WAYS

1 ASSUMED ANNUAL INVESTMENT RETURN

The 15.1 percent investment return exceeds the assumed 8 percent annual investment return. Part of PERA's legislative package for two consecutive years was a proposal to lower the assumption to 7.5 percent. After a special session last year, Gov. Mark Dayton vetoed the bill containing the lower assumption to 7.5 percent because of controversial provisions unrelated to the retirement systems. Investment return assumptions are based entirely on investment consultant forecasts for the future, not on short-term historical results. Lowering the assumed annual investment return to 7.5 percent is part of PERA's proposal for the 2018 legislative session (see related article on page 3).

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PRESIDENT'S MESSAGE

Kathryn A. Green
President
PERA Board of Trustees

This issue of the newsletter we highlight PERA's financial information. The news is good. The investment performance for PERA's three largest retirement plans for the fiscal year ending June 30, 2017 was excellent. For the 12-month period, the Combined Funds posted a 15.1 percent rate of return.

The 15.1 percent rate of return exceeded the assumed rate of return, other pension funds in the country, and investment management benchmarks for each asset class. The Minnesota State Board of Investment (SBI) invests PERA's financial assets. SBI pools the assets of the three statewide retirement funds into the Combined Funds.

It would only seem logical that with such a favorable investment return, that PERA would not need to seek plan design changes through legislation. This is simply not the case. The strong investment return did improve funding status for each plan. However, plan design prevents significant improvements in the funding status over the long term.

Before the PERA Board of Trustees voted on legislative proposals, PERA staff conducted extensive plan design analysis. Once initial legislative proposals were being developed, staff met with stakeholder groups to receive input. The stakeholder groups support the plan design proposals recommended by PERA, and the Board approved the legislative package. The proposal includes each plan and addresses changes aimed at a better plan design that will achieve the goal of full funding and the best way to deliver benefits to members.

PERA Board of Trustees has been proactive in proposing legislative changes to fulfill our important promise of providing sustainable retirement plans. The Board and staff continue to work to ensure the long-term financial stability of the retirement plans and provide services that our members value. That's our mission.

We have a long history proving that our plans can be sustained and will continuously monitor the direction of the funds and recommend changes when necessary to make sure they are sustained in the future.

Board approves legislative proposals for 2018 session

The 2018 retirement bill containing sustainability reforms for all Minnesota public pension systems was unani-mously passed by the Legislative Commission on Pensions and Retirement (LCPR) at their March meeting. The bill contains sustainability reforms for PERA's General, Police & Fire, and Correctional Plans. The PERA Board of Trustees unanimously approved the legislative proposals for the three retirement plans during their December and January board meetings. The Board also reaffirmed their position from last year to change the investment return assumption from 8 percent to 7.5 percent for future valuations. The Board agreed to the legislative pro-posals after PERA staff did extensive plan design analysis and met with various stakeholder groups since last summer to receive input on the legislative proposals. The stakeholders agreed and are actively supporting the plan design proposals recommended by PERA.

GENERAL PLAN

The legislative proposal adopted by the Board includes replacing the current cost-of-living adjustment (COLA) trigger structure with one tied more closely to inflation, or the Consumer Price Index (CPI). The current 1 percent COLA is not projected to trigger to 2.5 percent until 2045. To keep the change cost neutral, the annual benefit increase is proposed to equal 50 percent of CPI, with a floor of 1 percent and a cap of 1.5 percent on the actual increase payable. This would ensure annual increases no less than the current 1 percent and provide the possibility for an increase up to 1.5 percent if warranted by actual inflation rates.

THE LEGISLATIVE PROPOSAL ALSO INCLUDES:

- Extending the amortization period to 2048
- Eliminating the 1 percent post-retirement increase prior to the full retirement age
- Eliminating augmentation in the early retirement factors
- Eliminating augmentation for deferred members
- Reducing the interest rate on refunded contributions from 4 to 3 percent

Under the proposal the Plan's funding status will improve more rapidly, increasing the likelihood of long-term plan sustainability. The proposal does not require an increase in employee or employer contributions and will mean a more equitable post-retirement increase structure that is tied to actual inflation.

POLICE & FIRE PLAN

The Board voted to reaffirm their positions from last year related to changes to ensure the sustainability of the Plan. The changes were included in the vetoed 2017 Omnibus Retirement Bill.

The legislative proposal for the Police & Fire Plan includes removing the 2.5 percent trigger; increasing the employee and employer contribution rates by 1 percent and 1.5 percent respectively, phased in over a two-year time beginning Jan. 1, 2019; and changing to a 30-year amortization period.

The Board also voted to support additional funding, provided by the Legislature, to the Police & Fire Plan to ensure long-term financial stability.

CORRECTIONAL PLAN

The Correctional Plan legislative proposal includes a post-retirement increase to provide 100 percent of the Consumer Price Index (CPI), with a 1 percent floor, and a 2.5 percent cap until the Plan's funding ratio drops below 80 percent for one year or 85 percent for two consecutive years. The funding ratio would be measured on the market value basis every year. If the funding ratio does not meet the required level, the post-retirement increase would be 100 percent of CPI, with a 1 percent floor, and a 1.5 percent cap. Once the lower cap applies, no further triggers would exist.

The proposal preserves the opportunity for a post-retirement increase as high as 2.5 percent provided that the funded ratio exceeds the existing trigger.

2017 LEGISLATIVE SESSION

After a special session, Gov. Mark Dayton vetoed the bill containing the provisions relating to the PERA Police & Fire Plan, as well as other administrative changes. Changes to the PERA General and Correctional Plans were not included in the final version of the bill presented to the Governor. Changes relating to all of the Minnesota retirement plans were included in a bill that contained controversial provisions not related to the retirement systems.

STAY INFORMED

Visit mnpera.org for news about legislation during the 2018 session. The full Legislature must pass the bill and the governor must sign it before it becomes law. The 2018 legislative session ends May 21.

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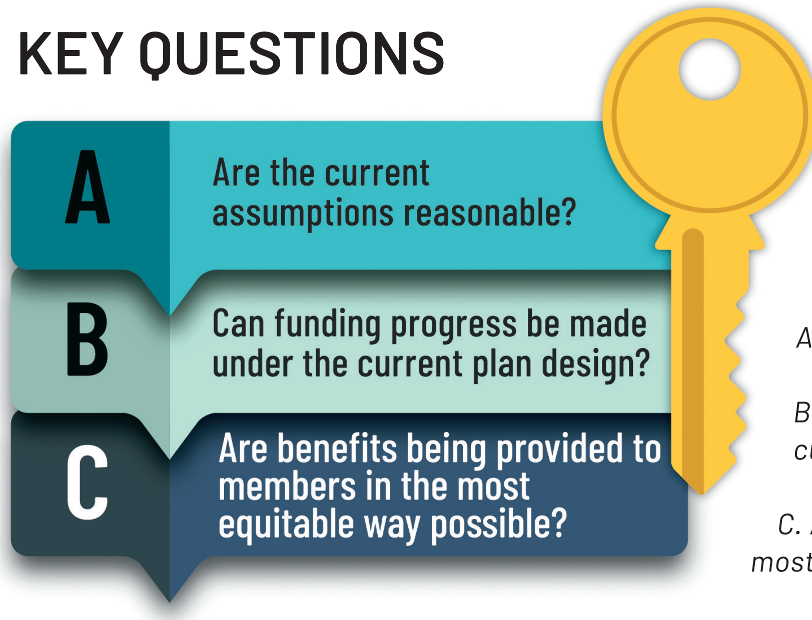
STRONG INVESTMENT RATE OF RETURN

2 NATIONAL INVESTMENT RETURN FOR PENSION PLANS

The 15.1 percent investment return exceeded the average return for public pension funds nationally for the period ending June 30, 2017. Nationally, public pension funds experienced a 12.4 percent return, as reported by Callan Associates. PERA's better-than-average result reflects the reward from a relatively more aggressive investment allocation taken by SBI during a period of time in which equity investment returns were positive.

3 SBI BENCHMARK

The third win for the 15.1 percent investment return was SBI achieved its goal to outperform a composite market index weighted to reflect SBI's long-term asset allocation policy. SBI's objective is to take advantage of the long investment time horizon offered by equities and alternative assets in order to meet its actuarial return target and ensure that sufficient funds are available to finance promised benefits at the time of retirement. The Combined Funds' performance is measured net of all fees and costs to assure SBI's focus is on true net return. On this basis, SBI has consistently outperformed the composite index by 0.2 percent over one, 10, and 20 years.



CHANGE IS STILL NEEDED

With the 15.1 percent investment return, the funding status for each plan improved. However, there is still a need for legislative changes to the plans. The main reason why there is still a need for legislative changes is that current plan designs prevent sufficient improvements in the funded status over time. Although the investment return provided funding improvement, the plans' design will not allow the investment return to significantly impact the funding ratio. The PERA Board approved a legislative package which includes each plan to address changes for a better plan design that will achieve the goal of full funding. The proposals for the General and Correctional Plans include lowering the investment return assumption from 8 percent to 7.5 percent, and replacing the current cost-of-living adjustment (COLA) trigger structure with one tied more closely to inflation, or the Consumer Price Index (CPI). For complete details on the legislative proposal for the 2018 session, see related article on page 2.

THE KEY QUESTIONS

In deciding on legislative action, the PERA Board of Trustees must ask three questions:

A. Are the current assumptions reasonable?

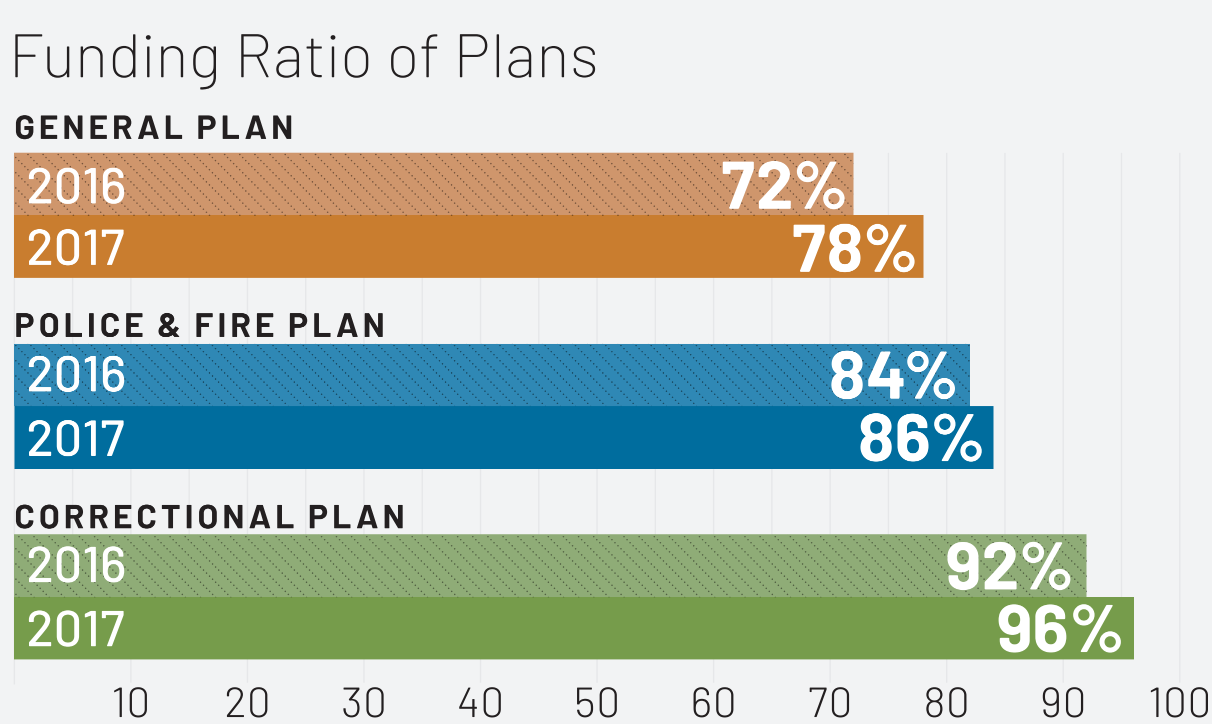
B. Can funding progress be made under the current plan design?

C. Are benefits being provided to members in the most equitable way possible?

If the PERA Board only considered funding status, it would be reasonable to take no legislative action. However, to get a complete picture, the Board must answer all three of these questions. When the answer is no to all the questions, then it is clear that legislative action is necessary to revise the assumption and have a way to improve funding progress and distribute benefits more equitably.

For more information on the funding ratio and how the current plan design impacts funding progress, see the article *The Basics of Pension Plans* below.

THE BASICS OF PENSION PLANS



WHAT IS FUNDING RATIO?

Funding ratio is a common measure of the funding status for a plan. How it works is that the higher the funding ratio, the stronger the financial health of the plan.

Using the current statutory investment return assumption of 8 percent to measure liabilities and the market value of assets, the funding ratio of all plans improved in 2017. The funding ratio of the General Plan increased from 72 percent to 78 percent; the Police & Fire Plan increased from 84 percent to 86 percent; and the Correctional Plan increased from 92 percent to 96 percent.

WHY THE DIFFERENCE IN PLAN FUNDING RATIO IMPROVEMENT?

The plans' funding ratio improvement varied because of differences in liability measurements. Both asset and liability changes impact the funding ratio of the plan. If all plans had equal assets and liabilities, and all other expectations were met, the funding ratio for each plan would have increased by about 7 percent from the 15.1 percent asset return (15.1 percent less the 8 percent assumed rate). The liabilities of all three plans increased by an amount more than expected, limiting further improvement of the funding ratio.

WHY THE INCREASE IN LIABILITIES?

For the General Plan and the Police & Fire Plan, there was an earlier expected benefit increase which created a larger liability. How the plan is set up, retirees would receive a 2.5 percent annual increase instead of 1 percent when the plan reaches 90 percent funding. The earlier benefit increases create a larger liability. As a result, asset increases—which move up the higher post-retirement date—are directly offset by liability increases due to that earlier date. Under the 8 percent assumption, the assumed date for the higher 2.5 percent annual adjustment moved from 2052 to 2035 in the General Plan and from 2050 to 2033 in the Police & Fire Plan. The 2.5 percent increase is already in place for the Correctional Plan.

USING 7.5 PERCENT INVESTMENT RETURN ASSUMPTION

Taking the same situation and using the recommended 7.5 percent investment return assumption to value plan liabilities, there is a small change in the funding ratio for the General Plan (78 percent to 76 percent) and no change for the Police & Fire Plan (86 percent). Generally a lower assumed investment return assumption would increase liabilities. The reason is that the opposite result of the improved investment performance plays a role. Because of the change in valuation, the assumed date for higher post-retirement increases is delayed (from 2035 to 2045 for the General Plan and from 2033 to 2066 in the Police & Fire Plan). The higher liability estimate is offset by corresponding lower benefits from the later date for the higher benefit.

GO GREEN WITH MY PERA

REGISTER TODAY

PERA mails more than 180,000 Personal Benefit Statements (PBS) each year. That's a lot of paper. Go Green with MY PERA. It's fast and simple to do. Register today.

MY PERA IS YOUR PERSONAL LINK WITH THE ASSOCIATION. HERE YOU CAN:

- Review and update your personal information
- View a current estimate of your benefits (just like your PBS), or create your own custom estimates
- Register for conferences and workshops
- Sign up for PERA's e-publications
- Adjust tax withholding and direct deposit once you begin receiving your benefit, as well as print out tax form 1099R and proof of income reports

WE'VE RECENTLY MADE UPDATES TO MY PERA. NOW YOU CAN:

- Add or update beneficiaries online (active and deferred members only)
- Create and view estimates including a non-spouse survivor (active and deferred members only)

NEED HELP?

We are here. If you registered with MY PERA and are not sure which email you used to create your account, contact us at 651-296-7460 or 1-800-652-9026. We can help you get back online.

Remember, we respect your privacy and will never share your email with third parties.

See related article about security updates to MY PERA.

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PERA's Comprehensive Annual Financial Report (CAFR) is available

PERA's Comprehensive Annual Financial Report (CAFR) is available online. The CAFR provides an extensive review of PERA's financial status, as well as information about PERA's structure, investments, and demographics.

PERA also released its Summarized Annual Financial Report. This is a summary of the CAFR highlighting PERA's mission and vision statements, a summary of the financial statements, along with a few interesting facts.

SECURITY UPDATES TO MY PERA

You can be confident that your MY PERA account is secure. We have recently made significant security updates to MY PERA for your protection. Members can no longer log in to your MY PERA account using your Social Security Number. You must now log on using your registered email address and password. To better protect your private data, MY PERA users will also go through an email verification process before they can access their online account.

BOARD DIRECTORY

The PERA Board of Trustees consists of 11 members. The State Auditor is a member of the Board by statute. Five trustees are appointed by the Governor to represent cities, counties, school boards, retirees and the public, respectively. The remaining five members are elected by the PERA membership at large to represent the general active membership, Police & Fire Plan members, and all benefit recipients. Board members serve four-year terms.

Watch for upcoming Board Election information

Kathryn A. Green, President
Appointed School Board Representative
Email: kathryn.green@mnpera.org

Thomas Stanley, Vice President
Elected General Membership Representative
Email: thomas.stanley@mnpera.org

Ross Arneson
Elected Retiree/Disabilitant Representative
Email: ross.arneson@mnpera.org

Paul Bourgeois
Elected General Membership Representative
Email: paul.bourgeois@mnpera.org

Mary Falk
Appointed Public Representative
Email: mary.falk@mnpera.org

Barbara Johnson
Appointed Cities Representative
Email: barb.johnson@mnpera.org

Leigh Lenzmeier
Appointed County Representative
Email: leigh.lenzmeier@mnpera.org

Rebecca Otto
State Auditor
Email: rebecca.otto@mnpera.org

Lori Volz
Elected General Membership Representative
Email: lori.volz@mnpera.org

Lawrence J. Ward
Appointed Annuitant Representative
Email: larry.ward@mnpera.org

Paul Ford
Elected Police & Fire Representative
Email: paul.ford@mnpera.org

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