

CITIZENS LEAGUE REPORT

No. 128

**Recommendations to improve the Public
Employees Retirement Assoc. (PERA)**

March 1961

Citizens League
545 Mobil Oil Building
Minneapolis 2, Minnesota
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APPROVED
BOARD OF DIRECTORS
DATE MAR 29 1961

TO: Board of Directors

FROM: Public Employment Committee, Charles H. Clay, Chairman

SUBJECT: Recommendations to improve the fiscal condition of PERA (Public Employees Retirement Association) and to provide improved employee benefits.

NATURE AND SCOPE OF ASSIGNMENT

The assignment given to the Public Employment Committee by the Citizens League Board of Directors was to "conduct research and make recommendations to assure maintenance of the fiscal soundness of the various municipal employee pension funds." This assignment stemmed from a general belief that many, if not all, of the various municipal employee pension funds are inadequately financed.

Public employees in Hennepin County, other than state and federal employees, are covered by the following six retirement pension funds:

1. PERA (Public Employees Retirement Association)
2. MERF (Minneapolis Employees Retirement Fund)
3. MTRA (Minneapolis Teachers Retirement Association)
4. MFDRA (Minneapolis Fire Department Relief Association)
5. MPRA (Minneapolis Police Relief Association)
6. Certain suburban police and firemen's retirement funds

The scope of the Public Employment Committee's assignment includes extensive review of various aspects of each of these six retirement funds. Our findings and recommendations will be submitted in a series of reports, of which this is the first.

The discussion and recommendations contained in this report concern themselves with (1) the adequacy of the funding of PERA, and (2) the desirability of coordinating PERA with the Old Age Survivors Disability Insurance (OASDI) program of the federal social security act.* PERA membership includes all employees throughout the state working at the county level of government and all municipal employees throughout the state, with the exception of firemen, policemen, teachers and Minneapolis city employees. Findings and recommendations involving the other five retirement pension funds, as well as those concerning PERA in the areas of investment of funds, composition of the retirement board, and retirement board procedures and policies are deferred to subsequent reports.

* Unless otherwise indicated, the term "social security" used throughout this report means OASDI.

RECOMMENDATIONS AND MAJOR CONCLUSIONS

Recommendations

1. The level of employer's contributions to PERA should be increased at the 1961 session of the Minnesota State Legislature sufficiently to assure that no further increase will occur in the existing deficit of \$141,500,000, as reported by the Public Retirement Study Commission. (Discussion on Page 8.)

2. Legislation should be enacted at the 1961 session of the Minnesota State Legislature establishing a coordinated PERA-Social Security program and authorizing present PERA members to participate in the coordinated plan. The enabling legislation establishing the coordinated PERA-Social Security program should:

- (a) Select the alternative which allows each present PERA member to elect on an individual basis whether or not to become a member of the coordinated program. All future employees would become members of the coordinated program on a mandatory basis. (Discussion on Page 16.)
- (b) Establish a benefit level comparable to that presently extended under PERA. This means following substantially the plan adopted in 1957 when SERA (State Employees Retirement Association) was coordinated with social security. (Discussion on Page 17.)

3. The Legislature should oppose any proposal which would increase the level of benefits under PERA until (a) PERA is placed on at least a frozen liability level of funding, and (b) a coordinated PERA-Social Security program has been established. (Discussion on Page 17.)

4. Legislation should be enacted at the 1961 session of the State Legislature authorizing in 1962 a new actuarial survey similar to the one conducted in 1958. These actuarial surveys should be repeated at least once every four years in the future. (Discussion on Page 8.)

5. Future increases in the level of benefits under the PERA portion of a coordinated program should (a) be accompanied by an actuarial report showing the cost of the proposed increase, and (b) provide for simultaneous increases in the level of contributions to the fund in an amount corresponding to level normal cost projections. (Discussion on Page 8.)

Major Conclusions

1. The Public Retirement Study Commission, a legislative interim commission assigned to study public employee retirement systems in Minnesota, has made an invaluable contribution to the people of Minnesota through the findings and recommendations contained in its reports to the 1957, 1959 and 1961 sessions of the State Legislature. We commend the members of the Legislature and the staff of this interim commission for the service they have performed. (Discussion on Page 6.)

2. The past and present level of PERA financing is inadequate. (Discussion on Page 7.)

3. The past practice of the Legislature of increasing the level of benefits without immediate and corresponding increases in the level of funding is unsound and should not be repeated in the future. (Discussion on Page 8.)

4. Periodic actuarial studies should be made and prompt action taken to maintain the PERA fund in actuarial balance on a level normal cost basis, and without further increase in the deficit. (Discussion on Page 8.)

5. PERA should be restored to its original concept of providing an annuity program for governmental employees with benefits based primarily on the amount of contributions made by the employee to the fund. The introduction into PERA of social insurance benefits, with emphasis on minimum adequacy rather than equity, should be discontinued. Social insurance benefits, such as disability, survivorship, and subsistence level retirement benefits, are more appropriately provided under the federal social security program. (Discussion on Page 9.)

6. None of the arguments raised against coordination of PERA with social security appears to be valid under a coordination plan which gives each present PERA member the right to elect whether or not to participate in the coordinated program. (Discussion on Page 14.)

7. Coordination of PERA with social security would result in a substantial reduction in the amount of the existing PERA deficit. (Discussion on Page 10.)

8. Coordination of PERA with social security would benefit public employees (PERA members) principally in the following ways:

- (a) Under a coordinated program, benefits to employees would at least equal, and in a substantial majority of cases would exceed, those now provided under PERA. (Discussion on Page 11.)
- (b) Public employees would retain accrued social security pension rights should they transfer to private employment, something not possible under the present PERA program. (Discussion on Page 12.)
- (c) Persons entering public employment at high ages who now cannot qualify for retirement benefits under PERA would be eligible for benefits under the more liberal social security provisions. (Discussion on Page 12.)
- (d) Survivorship benefits would not lapse in the interval between jobs in case of a transfer from public to private employment, or vice versa, as is presently the case under PERA. (Discussion on Page 12.)
- (e) Present members of PERA would be given the right to choose whether to retain coverage under PERA or to be covered under a coordinated PERA-Social Security program. This would assure each employee of the kind of retirement program which best fits his needs. (Discussion on Page 11.)

9. Coordination of PERA with social security would be beneficial to the employer (taxpayer) principally in the following ways:

- (a) Since employees in private industry who have accumulated rights under social security would be able to retain these accrued rights, it would be easier to attract qualified persons to public employment. (Discussion on Page 13.)
- (b) The future cost to the taxpayer of public assistance programs would be lessened. Many older employees not eligible for PERA retirement benefits would receive benefits under social security rather than under Old Age Assistance as presently is the case. Similarly, social security benefits to dependent children and widows would reduce the number of persons receiving public assistance. (Discussion on Page 13.)
- (c) The assessment of the cost of fringe benefits in arriving at a pay scale for public employees comparable to that paid those doing similar work in private industry would be greatly simplified, and a more equitable and exact pay formula could be established. (Discussion on Page 13.)
- (d) Persons who become public employees in the future would no longer be able to collect double benefits under PERA and social security. Presently, a significant proportion of public employees are or will become eligible for retirement benefits under both PERA and social security. (Discussion on Page 13.)

10. We concur in the policy adopted by Congress that coordination of PERA with social security is not to be used as a means of reducing the present general level of benefits under existing public employee retirement programs. We recommend a coordination plan which at the time of coordination would provide the level of benefits substantially as they are now. (Discussion on Page 17.)

GENERAL NATURE OF THE PROBLEM

The research project assigned by the Board of Directors to the Public Employment Committee was to review the fiscal soundness of the various pension funds covering public employees, other than those in federal or state employment, in Hennepin County. The following funds come within the scope of this assignment:

1. PERA (Public Employees Retirement Association)
2. MERF (Minneapolis Employees Retirement Fund)
3. MTRA (Minneapolis Teachers Retirement Association)
4. MFDRA (Minneapolis Fire Department Relief Association)
5. MPRA (Minneapolis Police Relief Association)
6. Certain suburban police and firemen's retirement funds

This assignment basically stemmed from a realization there is generally a significant inadequacy in the level of financial support of most of the above-named pension funds.

The pension funds being considered by the Public Employment Committee are supported jointly by contributions of employee participants and the governing unit (employer). Employees contribute in accordance with a formula fixed in each of the various retirement plans. In some instances the employer contributions are fixed by plan provisions; it is implicit, however, that the funding by the employer be adequate to provide for benefits to the extent that employee contributions and investment earnings are insufficient.

The funding requirements of any pension plan consist of two parts:

1. That part which is required to fund benefits accruing from employment service during a given year (referred to as level normal cost).
2. That part which is required to fund liability for benefits arising from employment in prior years.

To avoid an increase in the unfunded liability of any plan with a deficit contributions in an amount not less than the total of the interest on the unfunded deficit for prior service liability, plus the level normal cost from the current year's service, must be provided.* The Public Retirement Study Commission in its report to the 1959 session of the Minnesota State Legislature found

* This is known as the frozen deficit level of funding, and is recognized by the Committee as the minimum recommended funding level. The level normal cost of a pension plan may be thought of as the amount of money which must be set aside each year to cover the liability for the benefits accrued from employment service during that year, assuming that funds are invested in assets earning a determined rate of return, usually 3%. If the various assumptions used in valuing the plan liabilities are borne out by actual experience, the level normal cost will be a level percentage of covered payroll for all years in which the benefit formula remains unchanged. A plan is spoken of as being fully funded at a given time if the fund's assets equal the value of all future benefits which have accrued for prior employment service. The deficit is the excess of such liabilities over the assets.

that all of the above-named funds had deficits and, with the exception of the Minneapolis Teachers Retirement Fund, all were receiving support in an amount less than that required to avoid an increased unfunded liability. Because this inadequate level of contributions to these funds has persisted for many years, the unfunded liability has grown to a very substantial size. Unless this trend is reversed, taxpayers in future years will be compelled to increase substantially the level of contributions to these funds. The only other alternative would be to reduce the level of benefits to correspond to the level of contributions. We reject this alternative as unfair to the public employee.

SCOPE AND METHOD OF RESEARCH

Much of the Public Employment Committee's basic research and interviewing in handling this assignment was done through a subcommittee under the chairmanship of Boyd Mast. Other members of this subcommittee were Charles Clay, Thomas Beckley, Irving Keldsen, Justus F. Lowe, Sally Luther, Arthur D. Parsons, Orville Peterson, David Kennedy, and Walter J. Wheeler. The subcommittee first spent considerable time familiarizing itself with the contents of the 1957 and 1959 reports of the Public Retirement Study Commission. Next followed numerous subcommittee meetings held over a period of several months. Individuals considered to be experts on this subject were contacted personally and their views obtained.

The subcommittee decided that the assignment was far too complex to handle in a single report and that a series of reports should be submitted. PERA was selected for the first report because a proposal authorizing extensive changes in PERA seemed certain to be presented to the 1961 session of the Minnesota State Legislature.

DISCUSSION OF RECOMMENDATIONS AND MAJOR CONCLUSIONS

PUBLIC RETIREMENT STUDY COMMISSION COMMENDED FOR PERFORMING AN IMPORTANT SERVICE TO THE PEOPLE OF MINNESOTA

The Public Retirement Study Commission, established by the Minnesota State Legislature in 1955, consists of five members designated by the State Senate and five members designated by the House of Representatives. Its executive secretary is Frank V. Moulton, its consulting actuary is George V. Stennes and Associates, and its legal consultant is Joseph E. Hamilton.

The legislative act creating the commission gave it the following assignment: "The commission shall study the various retirement benefit plans available to employees of the State and employees of the various political subdivisions, political corporations, and school districts of the State, including within the scope of its enquiry the governing law, management, financial condition, and benefits of all such plans, any federal program for which such employees or any of them could be eligible, and such related matters as the commission deems proper for full legislative understanding and action."

The commission made its first report to the Legislature in January, 1957; its second report in January, 1959; and its third report has just been submitted. These reports have provided the public with its first real understanding of the seriousness of the fiscal condition of the various public employee retirement funds. In general, the commission's findings and recommendations have been

constructive and have provided the basis on which considerable legislation has been enacted to improve substantially the fiscal soundness of these funds.

The work of our committee would have been much more difficult had it not had the benefit of the reports of the Public Retirement Study Commission. The committee expresses sincere appreciation, on behalf of the Citizens League, to the Legislature for creating the commission, to the members who have served on the commission, and to the commission staff and actuary.

THE PAST AND PRESENT LEVELS OF PERA FINANCING ARE INADEQUATE

The first generally understood actuarial survey of the PERA fund came in 1956. This survey showed the condition of the fund as of June 30, 1955, to be as follows:

Unfinanced pension liabilities (deficits)	\$128,000,000
Annual rate of pension liabilities accruing to the fund	14% of reported payroll
Financial supports consisting entirely of members' contributions	4% of reported payroll

Thus the deficit was increasing at the rate of 10% of payroll, plus 3% interest on the previous deficit. Following the recommendation of the Public Retirement Study Commission, the 1957 session of the State Legislature reduced the benefit levels substantially and increased employee contributions to 6% of the first \$4800 of pay from the previous 4%; established a permanent level of employer's contributions at 6% of the first \$4800 of pay, as against the previous failure to contribute at all; and established an employer's contribution of 2.5% of the first \$4800 of pay as a means of financing the deficit. The total of these three types of contributions to the fund was 14.5% of the first \$4800 of pay.

An additional actuarial survey was made as of January 1, 1958. The Public Retirement Study Commission estimated the status of the fund as follows:

	<u>Jan. 1, 1958</u>	<u>June 30, 1959</u>
Accrued PERA liability	\$161,600,000	\$190,400,000
Assets	<u>26,100,000</u>	<u>48,900,000</u>
Unfunded liability (deficit)	\$135,500,000	\$141,500,000
Rate of level annual financing required to keep pace with currently accruing future liability	12.2% of pay	12.2% of pay
Rate of annual financing required to keep unfunded liability from increasing	<u>3.56% of pay</u>	<u>3.3% of pay</u>
Minimum annual support required to keep pace with annual growth of total liabilities of PERA	15.76% of pay	15.5% of pay
Rate of increased financing required to stabilize deficit	1.26% of pay	1% of pay

The \$128,000,000 deficit as of June 30, 1955 had continued to grow until it reached \$141,500,000 on June 30, 1959. It is clear, therefore, that the present rate of contributions to the fund is inadequate to prevent a continuing deficit accumulation.

THE LEVEL OF EMPLOYER'S CONTRIBUTIONS TO PERA SHOULD BE INCREASED AT THE 1961 SESSION OF THE MINNESOTA STATE LEGISLATURE SUFFICIENTLY TO ASSURE THAT NO FURTHER INCREASE WILL OCCUR IN THE EXISTING DEFICIT.

The exact amount of the increase in the level of contributions necessary to avoid incurring further deficits in the PERA fund will depend on what action, if any, the 1961 Legislature takes: (1) to authorize coordination of PERA with social security; (2) to increase investment income; and (3) to adjust benefit levels. For reasons discussed elsewhere in this report, the amount of the increase needed will be less if PERA is coordinated with social security.

If there is no improvement in the fiscal status of PERA in any of the above ways, then, according to the Public Retirement Study Commission's most recent projections, the required increase in order to avoid any further accumulation in the deficit would be from the present level of 14.5% to 15.5%, an increase of 1%.

Since the principal cause of this deficit condition has been the failure to make adequate employer contributions over the past many years, we believe the entire increase in the level of contributions should be borne by the employer (taxpayer).

LEGISLATION SHOULD BE ENACTED AT THE 1961 SESSION OF THE STATE LEGISLATURE AUTHORIZING IN 1962 A NEW ACTUARIAL SURVEY SIMILAR TO THE ONE CONDUCTED IN 1958. THESE ACTUARIAL SURVEYS SHOULD BE REPEATED AT LEAST ONCE EVERY FOUR YEARS IN THE FUTURE.

PERA had no adequate actuarial survey until 1956. If sound pension plans are to be established and maintained, there must be regular and thorough actuarial surveys. We believe the Public Retirement Study Commission's recommendation to have actuarial surveys every four years is sound. We urge the Legislature to authorize the next survey for 1962. We also urge that these surveys be conducted every four years in the future.

Equally important is the need for a projection of costs, calculated by a professional actuary, to accompany any legislation proposing an increase in the level of PERA benefits. No such cost projection has been required in the past, and there is no present requirement that bills under consideration by the State Legislature have such a cost analysis attached to them. A requirement of this kind would do much to avoid financial problems in the future.

We consider it essential that the level of contributions to the fund be increased whenever any legislation is enacted which increases the level of benefits. The amount of the increase should correspond to the actuarial projections of cost in accordance with the level normal cost theory of funding.

PERA SHOULD BE RESTORED TO ITS ORIGINAL CONCEPT OF PROVIDING AN ANNUITY PROGRAM FOR GOVERNMENTAL EMPLOYEES, WITH BENEFITS BASED PRIMARILY ON THE SALARY AND TENURE OF EACH EMPLOYEE.

PERA, when originally established and until recent years, was primarily an annuity retirement program with the benefits closely related to the amount of the employees' contributions over the years. This attention to equity rather than minimum adequacy is well conceived as an incentive to longer service and higher pay. As the federal social security program has developed, there has been a tendency to incorporate into PERA most of the social insurance features that have been made a part of the social security system. Examples of these features are disability benefits, survivorship benefits, and a subsistence level of retirement benefits. This represents a substantial departure from the concept on which the plan was inaugurated.

For a number of reasons it is much sounder to reconstitute PERA into an annuity program with benefits based on salary and tenure and to utilize the social security program for minimum adequacy social insurance benefits. These reasons are explained in detail elsewhere in this report.

FEDERAL ENABLING LEGISLATION MAKES COORDINATION OF PERA WITH SOCIAL SECURITY POSSIBLE.

In 1955 when the social security act was first enacted, many groups including employees of governmental units were specifically excluded from coverage. Since that time social security coverage has expanded steadily and is now mandatory for virtually all gainfully employed persons in the country, with the exception of employees of governmental units. In 1954, the social security act was amended by Congress so that, with appropriate action at the state or local level, employees of those governmental units could be brought into coverage under social security. Presently participants under the State Employees Retirement Association and all new participants under the State Teachers Retirement Association are covered automatically under social security as a result of action taken by members of these pension funds. This provision for coverage under social security, as it applies to public employees, is spoken of as social security coordination. It is designed by legislative enactment in such a manner that benefits provided from the retirement fund are reduced simultaneously with the coverage of the participant under social security benefits. In addition to the coordination of benefits, there is a corresponding coordination of contributions. Generally, benefits under the revised retirement plan are such that total benefits from the plan and social security will be comparable to those under the original plan. This requires a level of contributions to social security and the retirement plan which approximate those under the plan before coordination.

The Minnesota State Legislature in 1957 enacted legislation authorizing a vote among PERA members to determine whether they wished to become a part of a coordinated PERA-Social Security program. The employees rejected coordination at that time under a plan which required a favorable vote of a majority of all eligible PERA members. Had a majority of these eligible employees voted favorably, then all PERA members would have been brought under the coordinated plan on a mandatory basis.

Subsequently, Congress authorized an alternative method of coordinating public employee retirement programs with social security. This alternative would allow each PERA member as of the date of coordination to elect whether or not to

participate in the coordinated plan. If the member chose not to do so, then he would continue under the benefit and contribution provisions of the old PERA program. All future employees would be brought under the coordinated plan on a mandatory basis.

Legislation has been introduced at this session of the State Legislature which proposes coordination under this alternative plan.

A SUBSTANTIAL PROPORTION OF STATE AND LOCAL PUBLIC EMPLOYEES ARE NOW COVERED UNDER A COORDINATED SOCIAL SECURITY PROGRAM, AND THE PROPORTION IS STEADILY INCREASING.

Social security coverage for state and local governmental employees first became possible through an act of Congress in 1954. By 1957, approximately 2.2 million state and local governmental employees were covered under social security. This was approximately 14% of all state and local governmental employees throughout the country. The proportion has steadily increased since 1957 until today substantially more than 50% of all state and local government employees are covered under social security.

In Minnesota employees of the state elected to come under a coordinated SERA-Social Security program in 1957. Members of TRA (Teachers Retirement Association) became eligible in 1959 on an individual basis to participate in a coordinated TRA-Social Security program.

COORDINATION OF PERA WITH SOCIAL SECURITY WOULD BRING ABOUT A SUBSTANTIAL REDUCTION IN THE AMOUNT OF THE EXISTING DEFICIT.

Coordination of PERA with social security results in transferring some of the obligation for future payment of benefits from the PERA fund to social security. Since the PERA assets are not transferred to social security on a basis comparable to the liabilities, the net result is a decrease in the PERA deficit. The following purely hypothetical illustration demonstrates how the PERA deficit might be decreased through coordination. The figures used should in no way be construed as actuarial estimates of what will happen.

	<u>Status of fund before coordination</u>	<u>Status of fund after coordination</u>
Liabilities for accrued benefits	\$190,000,000	\$150,000,000
Assets	<u>50,000,000</u>	<u>50,000,000</u>
Deficit	\$140,000,000	\$100,000,000

Under the alternative plan where each PERA member would be allowed to elect whether to participate in a coordinated PERA-Social Security program, it is not possible to estimate accurately the extent to which the existing deficit would be reduced. We are certain, however, that coordination would reduce substantially the amount of the existing deficit and, in addition, would eliminate some duplication of benefits. One way to project the type of reduction in the PERA deficit that might be obtained under a coordinated PERA-Social Security program is to review what happened to SERA and TRA deficits following their coordination with social security.

Actuarial surveys indicated the SERA deficit immediately before coordination with social security to be \$45,900,000. Upon coordination, the deficit dropped to \$26,700,000, a decrease of \$19,300,000 directly resulting from coordination. A more recent actuarial survey showed the SERA fund to have a deficit of \$23,600,000, a further decrease of \$3,000,000. The Public Retirement Study Commission in its 1961 report to the Legislature stated: "SERA is the only one of the three major state pension funds now being financed at a rate sufficient to meet currently accruing liabilities and to steadily reduce the deficit resulting from past underfinancing. Continuation of this progress will be an excellent investment in soundness of the fund and long-range reduction in state costs." It is highly significant that the first state public employee pension fund to coordinate with social security is also the first state fund to reach a sound financial condition.

TRA (Teachers Retirement Association) was coordinated with social security by the 1959 session of the State Legislature. The 1961 report of the Public Retirement Study Commission shows that TRA had an unfunded liability of \$72,400,000 on January 1, 1958, prior to coordination. The report shows that the unfunded liability was reduced to \$60,300,000 by June 30, 1959. The report indicates the amount of reduction in the deficit which is attributable to coordination with social security as \$13,700,000. The commission stated, "It is significant that the reduction in the TRA unfunded liability (deficit) since 1958 is not the result of the annual financing through teachers' contributions plus state tax levies, but the reduction is due, primarily, to the 1959 repeal of the 'second savings clause' and the enablement of coordination with social security." (Emphasis supplied.)

There is every reason to expect a reduction in the deficit comparable to that attained under coordination of TRA with social security through coordinating PERA with social security.

COORDINATION OF PERA WITH SOCIAL SECURITY WOULD BENEFIT PUBLIC EMPLOYEES (PERA MEMBERS).

Under the type of coordinated PERA-Social Security plan where each employee would be allowed to elect whether to participate in the coordinated plan, no present employee would receive any financial disadvantage. If any employee found it disadvantageous to participate in the coordinated program, he could continue to retain and accrue all benefits under the present PERA program.

Generally, the level of annuities under the coordinated plan would at least equal and in most cases exceed those presently being paid under PERA. For example, if the level of benefits adopted under the coordinated SERA-Social Security plan were followed for PERA, any public employee who had not been in public employment for ten or more years as of 1957 now receives a smaller retirement annuity for all periods of allowable service up to 35 full years than he would under the coordinated plan. This is true at all levels of average earnings, including the maximum. At the \$250 per month average income level, the PERA retirement annuity becomes equal to the SERA-Social Security annuity only after 42 years of allowable service. The greatest discrepancy occurs at the 5-20 year period of service. For ten years of service, PERA provides from \$20 to \$40 monthly annuity payments, while SERA-Social Security provides from \$96.50 to \$149. At fifteen years, the range is \$40-80 under PERA as compared to \$105.25 to \$109.50. At twenty years, the PERA range is from \$60-\$120 per month, compared with SERA-Social Security's range of \$114 to \$185. Thus, it may be seen that any relatively new or young PERA member would be substantially better off under a coordinated PERA-

Social Security program. This assumes, of course, that the employee will not become eligible for double benefits under both PERA and social security.

One of the greatest advantages of a coordinated PERA-Social Security program is the continuity of coverage which would be provided and which is so seriously lacking today. For example, under a coordinated program any public employee who transfers to work in private industry would retain all accrued social security pension rights. Under the present PERA program, any public employee who leaves public employment during his first ten years acquires no annuity rights and receives only a refund in the amount of his own contributions to the fund. Somewhat the same situation holds true with respect to transfers between different levels and units of government. Similarly, there would be no lapse in disability or survivorship coverage to an individual who transfers from public to private employment, or vice versa, or from one governmental unit to another.

A coordinated program, where tried, has generally contributed to improved employee morale. It is easier to project the level of social security benefits years in advance of retirement than it is present PERA benefits which depend somewhat on promotions. Employees seem to prefer a "basic" retirement program which can be planned for and to supplement this with an annuity program which would be more closely related to salary and tenure.

Because of liberal qualification provisions of the social security program for older persons, immediate coordination of PERA with social security would make pension rights available to many persons who enter public employment at a high age and who presently would not be eligible for retirement annuities on reaching retirement age. PERA provides no retirement annuities for persons with less than ten years' service, in contrast to employees in private industry who can qualify for social security retirement benefits after only a relatively few quarters of employment credit. It is becoming increasingly difficult to attract to government employment persons at middle or older ages because they usually jeopardize accrued social security benefits.

Because of the many variables it is difficult to compare the survivorship benefits provided under PERA with those which would be provided under a coordinated PERA-Social Security program. Considerably different benefit payments are provided to a surviving widow and/or child in case of the death of the employee. Under PERA the widow receives benefits for the balance of her life, while under the coordinated program she would receive benefits during the time she has minor children and after age 62. However, the amount of the benefit received is substantially higher under the coordinated program in most income categories. Under the coordinated program, the benefit level is tied to the average earnings of the deceased employee, whereas under PERA the benefit level is substantially the same irrespective of average earnings. Also, the coordinated program would provide benefits for a dependent parent, while PERA does not.

Under PERA, the disabled employee receives a monthly benefit based on service, average salary and age when disabled. He gets the same amount irrespective of the number of dependents he has. Under the coordinated program, the employee and his dependents would receive a social security family benefit which would be the same as that which they would receive upon retirement at age 65. In general, the benefits under PERA-Social Security are more generous in most instances whether the disabled employee has one or more dependents.

Under PERA, if death occurs after retirement, the only death benefit payable under the normal annuity is for the month of death, plus \$250. In order

to avoid this possible hardship, the employee has to elect an actuarially equivalent annuity which would provide either a joint or survivorship annuity or an annuity with a period certain. Election of these options results in a substantial reduction in monthly annuity benefits to the retired employee. Failure to choose one of these two options results in no protection for his family from the time of his death. The coordinated PERA-Social Security plan would provide the same survivor benefits to the family whether the employee dies before or after retirement. In the case where the employee dies after retirement leaving a family, the coordinated plan benefits are clearly superior.

In general, the emphasis of the social security program on adequacy rather than equity appears to provide a superior basic benefit program to public employees where the benefits are most needed. This then would be supplemented by the PERA annuity program based principally on salary and tenure.

COORDINATION OF PERA WITH SOCIAL SECURITY WOULD BE BENEFICIAL TO THE EMPLOYER (TAXPAYER).

Coordination of PERA with social security would make comparison of wage levels in private industry and in public employment much easier for the purpose of providing equitable wage and salary levels. Since the basic level of retirement, disability and survivor benefits would be the same for private and public employees, the costs would be identical. This would permit computing the cost of the PERA portion of the coordinated program and computing the cost of supplemental programs in private industry for employees doing substantially the same work, thereby making it easier to arrive at equitable salary levels. Making this comparison today under such different benefit programs is all but impossible.

As indicated earlier in this report, the fact that coordination would bring about a substantial reduction in the existing PERA deficit would inure to the benefit of the Minnesota taxpayer. As also discussed elsewhere in this report, a coordinated program would attract qualified prospective public employees of middle or older ages who now are unwilling to jeopardize their accrued social security benefits.

Minnesota taxpayers would also benefit to the extent that retired public employees no longer find it necessary to go on the old age assistance rolls. The coordinated program would provide immediate retirement and survivorship benefits for many persons presently on public payrolls who will not be eligible for these benefits under present programs. In the absence of a coordinated program, these people will, in many instances, have to apply for old age assistance, the cost of which is borne by the general taxpayer.

A coordinated PERA-Social Security program would benefit the general taxpayer in two other respects. First, as a participant in the social security program, and, second, as a Minnesota taxpayer who contributes a major portion to the cost of the present PERA program. This would occur because, under a coordinated program, future public employees would not be able to qualify for substantial retirement benefits under two pension programs. At the present time employees who have either completed their public service or who are in part-time work covered by social security can qualify for retirement benefits under both social security and PERA. As a consequence, the public generally is required to contribute to financing duplicate pension programs for these employees. The social security program allows relatively easy eligibility for benefits by emphasizing minimum

adequacy rather than equity, and it is unfair to the long-term social security employee to have to provide benefits of this kind to retired public employees in the form of a supplement to their own program rather than as a basic minimum type of pension program. In addition, the ability to leave public employment at a relatively young age and become eligible for social security benefits in addition to PERA benefits encourages public employees to leave public employment before reaching retirement.

NONE OF THE ARGUMENTS RAISED AGAINST COORDINATION OF PERA WITH SOCIAL SECURITY APPEARS TO BE VALID UNDER A COORDINATION PLAN WHICH GIVES EACH PRESENT PERA MEMBER THE RIGHT TO ELECT WHETHER OR NOT TO PARTICIPATE IN THE COORDINATED PROGRAM.

We have attempted to collect all the arguments or objections raised against coordination of PERA with social security. Each of them is stated below, followed by what appears to us to be a valid counter argument:

1. The social insurance or welfare state characteristics inherent in the social security program are unsound. This argument was raised in 1935 when the social security program was first enacted and has been voiced ever since. This objection has steadily diminished both in intensity and in the number of people making it to a point where today the vast majority of our people accept the need for a minimum social insurance program based on adequacy rather than equity. An attempt in Congress to abolish social security today would find almost no support.
2. Although social security might be all right for employees in private industry, it is not suitable for those in public employment. We reject this argument as having no basis in fact. On the contrary, we regard social security as a proper program for all employees unless the group can demonstrate reasons why they should be made an exception. The burden of proof should be on those who resist coordination, not on those who propose it. Employees in private industry have the same needs upon retirement as those in public employment, and vice versa. Coordination in no way precludes public employees from having their own annuity program as an addition to the basic social insurance program. Were there a valid distinction, then public employees should not be permitted, as they do presently, to receive social security benefits in cases where they become eligible under both programs.
3. Accrued rights of public employees toward retirement programs should not be taken away nor tampered with. This argument cannot be sustained under the coordination plan proposed which would allow each present employee to elect whether or not to participate in the coordinated program. Those who elect to refrain from participating in the coordinated program will continue to have the same benefit rights they do at the present time.
4. The coordinated program would place costs and benefits beyond the control of the State Legislature. The kind and level of benefits and the cost of the PERA program are now, for all practical purposes, beyond the control of the State Legislature. Whenever Congress increases or changes benefits under the social security program, there is an immediate attempt -- usually successful --

to provide similar benefits under each of the public employee retirement programs. Almost all of the recent legislative changes increasing the level of PERA benefits, for example, have been patterned after social security changes. Therefore, there is convincing evidence that public employees will, in one way or another, receive benefits substantially similar to those granted under the social security program.

5. The projected cost of a coordinated PERA-Social Security program is higher than that for the present PERA program. It is true that the projected level normal cost of PERA is 12.2% of payroll, as against a projected cost of 15% of payroll in 1969 for the coordinated program. But as demonstrated elsewhere in this report, the benefits provided under the coordinated program in most instances are more beneficial to the public employee. Also, there is no assurance whatsoever that the level normal cost of PERA will remain constant at 12.2% of payroll. In fact, there is every indication based on the historical pattern that the cost will increase. In view of the existing deficit condition of the PERA fund, we have already reached a point where contributions must be at a rate of about 15% of payroll just to keep the deficit from growing. There is little to justify any conclusion that costs will be significantly different whether or not coordination takes place.
6. It is unfair to compel future public employees to participate in the coordinated program without giving them the same right to elect as is given to present employees. We should not forget that, other than for public employees, almost no one has had the privilege of deciding whether or not to come under social security. Coverage has been mandatory in almost all instances. Therefore, it could be argued that the right to elect given to present public employees is in the nature of a privilege granted to very few others. Justification for granting this privilege to present employees is that it is somewhat unfair to change the rules of the game on employees who have come to count on a certain pension program. This would not be true in the case of future employees, because they would know at the time they decided to enter public employment exactly the pension program for which they would be eligible. This argument seems somewhat academic, in any case, as the benefits under the coordinated program are such that almost all new employees would doubtless elect to participate in the program anyway.
7. Coordination of PERA with social security means, for all practical purposes, the end of the PERA program. This conclusion cannot be justified by the facts. Public retirement portions of coordinated programs in other states have not only continued in existence, but have expanded in recent years. The same can be said for supplemental retirement programs in private industry where the rate of expansion of benefit levels has been speeded rather than retarded since social security was established.
8. It is impossible to depend on the social security program -- it is in a constant state of flux. It is true that frequent changes have been made in social security benefits over the years, but without exception each change has been in the direction of providing more

generous benefits. There isn't the slightest sign that this trend will be reversed. In any event, there has been little stability in PERA benefits during recent years either.

9. Female public employees would be compelled to contribute to social security disproportionately to the level of benefits they will receive. There is no question but that many of the benefits provided under social security are of little or no advantage to women. However, any unfairness that exists in this respect is no greater than it is for women in private industry. The introduction of survivor and disability benefits into the PERA program in recent years has placed women in substantially the same position as they would be under a coordinated program. Any program which is based on the concept of providing a minimum level of benefits where most needed is subject to this criticism.

LEGISLATION SHOULD BE ENACTED AT THE 1961 SESSION OF THE MINNESOTA STATE LEGISLATURE ESTABLISHING A COORDINATED PERA-SOCIAL SECURITY PROGRAM AND AUTHORIZING PRESENT PERA MEMBERS TO PARTICIPATE IN THE COORDINATED PLAN.

In order for PERA members to elect to participate in a coordinated PERA-Social Security program, the State Legislature must take action to fix the specific coordination plan and establish the procedures under which employees can elect to be covered. We strongly recommend that this legislation be enacted at the 1961 session.

Some argue that coordination of PERA with social security should be delayed until there is an opportunity to gain additional experience under the coordinated plans now operating for state employees and state teachers. We reject this argument. More than half of all state and local employees throughout the nation are now covered by social security. The Minnesota State Legislature by acting in 1961 would not in any way be pioneering in this field. Imperfections which might become apparent after experience with the coordinated plan can be worked out in future legislative sessions. The hardships which might arise from a few imperfections are minor compared to the hardships which most certainly will arise through delay. We particularly refer to the hardship confronting those public employees nearing retirement age who are not now eligible for any retirement program.

THE ENABLING LEGISLATION ESTABLISHING THE COORDINATED PERA-SOCIAL SECURITY PROGRAM SHOULD SELECT THE ALTERNATIVE WHICH ALLOWS EACH PRESENT PERA MEMBER TO ELECT ON AN INDIVIDUAL BASIS WHETHER OR NOT TO BECOME A MEMBER OF THE COORDINATED PROGRAM.

With very few exceptions all employees in private industry were brought under social security coverage on a mandatory basis. They had no option. Aside from the merits, however, there is no way under existing enabling legislation to bring about mandatory coverage of public employees. On the contrary, the only way public employees can be brought under a coordinated social security program is with their consent under either of two alternatives.

Section 218 of the Social Security Act describes the manner in which employees of local and state governments may obtain coverage under social security. State enabling legislation can be designed under one of two plans: (1) a plan whereby a majority vote of the affected employees is required and, upon at-

taining such a majority all employees, present and future, are mandatorily covered under social security from the date prescribed in the act, and (2) a plan whereby all future employees in the group are covered under social security as a mandatory condition of employment and whereby present employees elect to come under or stay out of social security. Persons covered under SERA came in under the first of the two plans, and persons covered under the State Teachers Retirement Plan came in under the second or optional plan.

Although there is considerable merit to the first of these two coordination alternatives, the practicalities of the situation would seem to dictate that the optional plan is the only politically feasible approach under which public employee groups are likely to be covered under social security. We believe the advantages of assuring that all future PERA members will be covered under the coordinated PERA-Social Security plan outweigh any disadvantages which might result from giving each present employee the right to elect whether to participate in the coordinated plan.

COORDINATION OF PERA WITH SOCIAL SECURITY SHOULD NOT BE USED AS A MEANS OF REDUCING THE PRESENT GENERAL LEVEL OF BENEFITS.

Our purpose in recommending coordination of PERA with social security is not to reduce the existing level of benefits under PERA. Our objective is to recommend a more suitable total pension program for public employees. Congress, in establishing enabling legislation permitting public employees to come under social security, rejected any attempt to use coordination as a means of reducing existing public employee retirement benefits. It is doubtful that any coordination plan which had as its objective reduction in the level of benefits would obtain the approval of the social security administration. Furthermore, any such reduction would be impractical under enabling legislation permitting each present public employee to elect whether or not to participate in the coordinated program.

We recommend a coordination plan which would leave the level of benefits substantially as they are now. This general plan was used when SERA was coordinated with social security in 1957. This meets the Congressional requirement, and, in addition, is fair to long-term public employees who have come to rely on a given level of retirement benefits.

THE LEGISLATURE SHOULD OPPOSE ANY PROPOSAL TO INCREASE THE LEVEL OF BENEFITS UNDER PERA UNTIL (1) PERA IS PLACED ON AT LEAST A FROZEN LIABILITY LEVEL OF FUNDING, AND (2) A COORDINATED PERA-SOCIAL SECURITY PROGRAM HAS BEEN ESTABLISHED.

In view of the serious deficit condition of the PERA fund, the argument is compelling that there should be a requirement that its fiscal house should be put in order before any further increase in the level of benefits is considered. If it is not possible to bring the fund into more adequate balance before embarking on further increases in the level of benefits, then the future condition of the PERA fund is indeed serious and can only deteriorate further.

We regard coordination of PERA with social security as so important to a sound total pension program for public employees that any further increase in the level of PERA benefits should be postponed until PERA is coordinated. Only by such a harsh prohibition on expanded benefits can the prospects for coordination be maximized. Only after coordination is effected can we intelligently determine the direction that increased benefits should take. We believe a "hold the line" attitude at this time will work to the best long-range interests of PERA members as well as of the taxpayer.