

June 20, 1990
Room 15 Capitol

1st Subcommittee Meeting



LEGISLATIVE COMMISSION ON PENSIONS AND RETIREMENT

ACTUARIAL SERVICES SUBCOMMITTEE

MINUTES

Senator Steven Morse, Chair of the Actuarial Services Subcommittee, called the meeting to order at 1:20 P.M.

Subcommittee members present:

Senators Steven Morse, Earl Renneke and Gene Waldorf
Representatives Robert A. Johnson, Gerald Knickerbocker and Leo Reding

Senator Morse began the meeting by stating that he had requested that Lawrence A. Martin, Executive Director of the Commission, put together some information explaining what is required in current statute in comparison with the Solon/Johnson bill and compare both of those with the recommendation by the previous actuarial services subcommittee. This new Subcommittee's objective is to look at the issue of the Commission actuary without regard to a particular vendor, what should be done in contracting for actuarial services, and what services should be provided. Sen. Morse went on to say that the Subcommittee was doing this as a parallel action to the possible review of the billing practices of the Commission actuary by the Legislative Audit Commission.

Sen. Morse introduced Mr. Martin to review the materials he had prepared. The materials included a memo dated June 14, 1990, which provided a brief background on the provision of actuarial services and a comparison of the approaches to the provision of actuarial services that have come out of the 1990 Legislative Session. The materials also included a copy of current statutes pertaining to the provision of actuarial services, the Solon/Johnson bill introduced in the 1990 Session, and the recommendations of the previous actuarial services subcommittee.

Sen. Renneke asked if the current status of the statutes had changed considerably from what was enacted in 1984. Mr. Martin responded that major changes affecting how the Commission actuary functions took place in the 1987 Session. A number of the changes were of a technical nature clarifying things like the role of the Commission actuary, setting optional annuity forms and early retirement factors. Another major change in the 1987 Session, was the implementation of a procedure allocating the costs for the actuarial valuations and experience studies to the various pension funds.

Sen. Renneke then asked if things have changed for the pension funds since the enactments of 1984. Mr. Martin responded that he was aware, from receiving full actuarial valuations performed by other actuaries that parallel work is being provided to some of the pension funds.

Sen. Renneke asked the Chair to request that the different pension funds respond to the question of what changes have occurred for them since enactment of the 1984 legislation.

Rep. Johnson noted that since 1984 there has been duplication of some services but the Pension Commission paid all of the Commission actuary's fees. In 1987, however, the fees were shifted to the pension funds. He also asked for a response from the pension funds.

Sen. Renneke stated that if the only reason for requesting a change was based on who was paying for the services then that was not enough of a reason to change. He wanted to know the policy questions, outside of the funding, behind the request for a change.

Rep. Reding asked Mr. Martin if it was correct that statute did not give the Commission actuary the responsibility for costing out benefit increases. Mr. Martin responded that this item is not specifically provided for in statute but the general practice has been that the Commission does receive information from its actuary on those matters.

Sen. Morse asked Mr. Martin to review the two proposals presented to the 1990 Legislature and note which changes could be made without changing statute and which changes can only be made by changing statute. Mr. Martin responded that, more often than not, the changes would require changing the statute. Mr. Martin went on with the review and noted that the basic approach of the Solon/Johnson bill is to return to the pre-84 method with little change in the actuarial services to be provided. The prior subcommittee proposal's approach is to retain the Commission actuary with primary responsibility for providing actuarial services and to reduce the services provided. Mr. Martin went on to compare the two proposals.

Sen. Morse asked Mr. Martin what changes contained in the Solon/Johnson bill could be accomplished without changing statute. Mr. Martin responded that the major thrust of the Solon/Johnson bill could only be accomplished by changing statute.

Sen. Morse stated that the subcommittee's responsibility was to look at what should be done about an actuary since it is the statutory responsibility of the Commission to have an actuary in place to provide the valuations by a particular date. Discussion followed.

Sen. Morse asked Mr. Martin to continue with his review of the two proposals. Mr. Martin stated that the prior subcommittee proposal would reduce the required actuarial services to a minimum, change the method of allocating the fees of the Commission actuary to the various funds from the current method, which is based

on the relative size of the fund from a membership standpoint, to a procedure allocating the fees based on a percentage which more closely reflected the work required for a particular pension fund, increase access to the actuary by the funds, and establish a permanent advisory committee to the Pension Commission on the topic of actuarial services. Many of these changes also require statutory changes.

Sen. Morse asked how the allocation of fees based on percentages would be calculated. Mr. Martin suggested that Mr. Robert Perkins, Commission actuary, respond to the particular percentages. Mr. Perkins explained how this could be accomplished based to some extent on the actual cost of doing each fund's valuation, with other considerations also taken into account, to produce a percentage, based on The Wyatt Company's five years of experience with this work, that would be equitable to all of the funds.

Sen. Renneke asked what is the Subcommittee's role? Is it to determine what flexibility the Commission has during this interim and/or to develop legislation for next session?

Sen. Morse responded that the primary role is to address the immediate needs for this year but added that these issues would be out there for the next session.

Sen. Waldorf commented that he believed the purpose of this Subcommittee was to come to some resolution between both proposals as well as to address the immediate needs.

Rep. Johnson agreed with Sen. Waldorf and commented that he thought Sen. Renneke had some legitimate policy questions. He also noted his concern about the June 30 contract expiration and what the contract would contain. He believes there is some flexibility on whether the Commission must have an actuary on July 1.

Sen. Morse stated that he was not clear in his direction from the Commission Chair as to whether the Subcommittee was to come to some resolution on the whole package covering the legislative changes or just address the immediate needs of the Commission regarding its actuary. Sen. Morse went on to ask Rep. Johnson if he had anyone in particular he would like to have testify. Rep. Johnson responded that he would like Paul Groschen to testify first.

Paul Groschen, Executive Director of MSRS, began by commenting that the major policy issue is that Minnesota taxpayers are paying too much for actuarial services. Mr. Groschen went on to state that the fund directors cannot fulfill their fiduciary responsibility with the Commission actuary, they need to hire their own actuary. MSRS requested a response from The Wyatt Company regarding mortality tables and early retirement tables that took six months to receive. Mr. Groschen went on to note that he currently values the State Patrol Plan and the Judges Plan, he does not value the Unclassified Plan, and he does not have statutory authority to value the Legislators Plan or the Elected State Officers Plan, however, he would have that authority in the Johnson/Solon bill. It is Mr. Groschen's view of current statute that the Commission needs to hire an actuary sometime in the fiscal year and must have a valuation performed by the Commission actuary before next session.

Sen. Waldorf asked why Mr. Groschen believes he cannot fulfill his duties unless he can hire his own actuary. Mr. Groschen responded by saying MSRS's actuary must be accountable to MSRS not to the Commission. He does not believe the actuary can be accountable to both. Sen. Waldorf stated that he didn't see a conflict of interest, an actuary has professional responsibilities to do what they're licensed to do as does a lawyer or other professional. Discussion followed.

Rep. Reding asked about a State Patrol 1.3 error. Mr. Perkins responded by stating that after publishing the current State Patrol actuarial valuation, the MSRS actuary contacted The Wyatt Company and stated that they came up with a different number for the State Patrol. Wyatt checked and found that in 1985, when Wyatt first set up their program, there was an error in Wyatt's calculations but after five years of auditing this was the first time it had been raised. Discussion followed.

Sen. Morse stated that this issue would not have come up if the Pension Commission was still paying the fee for the actuarial services as was the procedure before 1987. Mr. Groschen responded that was correct. Discussion followed.

Sen. Waldorf asked how the two actuaries access the MSRS data. Mr. Groschen responded that they come to an agreement as to what the tape records are supposed to contain. They then send a tape to both actuaries and the two actuaries coordinate with each other so that they have tapes that are identical. Sen. Waldorf then asked if there was cost duplication as a result of accessing the data. Mr. Groschen responded that the cost was minimal. Sen. Waldorf asked Mr. Perkins, if the MSRS actuary costed out a benefit proposal, could Mr. Perkins properly analyze the results without actually costing it out as well. Mr. Perkins said that if the benefit increase was very simple, they could analyze the results but this would be very difficult to do in the case of the recent benefit increase proposals or the Rule of 85 proposal.

Sen. Morse requested additional comments or testimony from the fund directors.

Elton Erdahl, Executive Director of TRA, stated that he is basically in agreement with Mr. Groschen. He believes, as a matter of principle, the pension funds have a fiduciary responsibility to have an official valuation conducted of the funds and further that the pension funds should have the authority to hire an actuary through a competitive bidding process, pay the actuary and have the actuary directly responsible to the pension funds. This is what they support. The Commission actuary would then have the responsibility to

audit and verify the pension funds actuarial work, set the actuarial standards, approve any changes in assumption rates, etc. If the Commission actuary does the valuation and the pension fund actuaries audit them, the pension funds are paying for the Commission actuary's valuation and for the audit. If the Pension Commission was paying for the Commission actuary's valuation, as was the case prior to 1987, the pension funds had fewer complaints.

Sen. Morse asked Mr. Erdahl who would pay for the Commission actuary's audit in the Solon/Johnson bill. Mr. Erdahl responded that it was his understanding that the Commission would pay for the audit. Discussion followed.

Sen. Waldorf asked if Mr. Erdahl's position was that the funds need their actuaries to do their bidding and pay for that service out of the pension fund and the Commission's oversight requirement should come out of the general fund. Mr. Erdahl responded that was correct. Sen. Waldorf stated that throughout the Legislature, where oversight is required, the cost of that oversight is charged back to the agency the Legislature is overseeing. For example, the Pollution Control Agency is funded in large part by the people they are overseeing, the Medical Practices Board is funded by the profession, and, in most instances where the Legislature is providing oversight, the bill is paid by those groups.

Rep. Johnson stated that these points are worthy of discussion, however, the charges for the Pension Commission's actuary have only been allocated since 1987. Discussion followed.

James Hacking, Executive Director of PERA, stated that he agrees with the previous fund directors. Mr. Hacking went on to state that statutes specifically assign fiduciary responsibility to the pension fund boards. As fiduciaries, the boards have to keep track of the financial condition of the funds and to do that they have to perform and be responsible for an actuarial function as well as other functions such as accounting functions, benefit calculation functions, etc., all of which the statutes assign to them. The Commission has a basic responsibility to do what is necessary for the integrity of the system overall. The question is not whether there is duplication, the question really is how much duplication is necessary for the various parties to carry out the roles that they are assigned. The pension funds are concerned with rising costs and the lack of accountability. The fund directors did not complain about the cost of the Commission actuary's services prior to 1987 because they were not paying any of the costs for the Commission actuary's services. Once they had to pay, they began to look at the reasons those costs were so high. He believes the terms of the current contract and the recommendations from the Commission actuary and approved by the Commission are responsible for the rise in the cost of actuarial services. He would be willing to go to his board and recommend payment of PERA's fair share of an audit and periodic experience study by the Commission actuary. He agreed that whatever action the Commission takes would require changing statute.

Sen. Waldorf noted that part of the reason PERA's allocation of the Commission actuary's fee is so high is due to the statutory method of allocating the fee. He agreed that PERA's share of the cost is inappropriately large.

Sen. Morse asked if Mr. Hacking knew what PERA's share of the cost would be under the prior subcommittee's proposal. Mr. Hacking responded that he believed there would be a reduction but not as much as it appeared because of the additional cost of recoding, reprogramming, different methods of data gathering, and the added responsibility to generate different schedules that the Commission actuary now generates. Sen. Morse noted that in the summary of the actuarial subcommittee's proposal, the PERA proposed allocation cost would be \$28,000.

Sen. Waldorf noted that the prior subcommittee proposal included some significant reductions in the services of the Commission actuary. The subcommittee made an effort to respond to what services the Commission needed to perform its oversight function. Discussion followed.

Rep. Reding stated that if there is an error in the calculations of a proposal or if a proposed benefit increase causes an unfunded liability, the Legislature is requested to respond. He asked Mr. Hacking if that was correct. Mr. Hacking responded that the Solon/Johnson bill provides that the Commission actuary would be able to cost out and cross check the cost of benefit improvements. If one of the funds comes in with a proposal that may have a significant impact on costs, everyone benefits by having an independent review of it. Rep. Reding stated that in reality, the 89 benefit package came in at the last hour, no one was in a position to make the assessments as to the cost of that benefit package, perhaps the effective date of benefit packages should be delayed one year to permit the actuary time to assess the package.

Sen. Waldorf stated that statutory changes would be necessary and hoped that all concerned parties could agree on what would insure the Commission of adequate oversight.

Rep. Johnson stated that he believed the Subcommittee has a responsibility to look at a short term contract to satisfy the Commission's statutory obligations and then suggested that the Subcommittee make recommendations to the full Commission for the 1991 Legislative Session.

Sen. Morse agreed with Rep. Johnson and stated that perhaps the two step approach should be considered.

The meeting adjourned at 4:15 P.M.