Teachers Retirement Information Bulletin

Retiree Edition ■ Winter 2015

Duluth Teachers merger underway

TRA has been busy since summer getting ready to bring 837 active, 1,502 retired, 1,630 deferred Duluth educators, and one new employer into the statewide fund.

Duluth Teachers Retirement Fund Association (DTRFA) assets are being transferred to the Minnesota State Board of Investment. Duluth teachers officially will become members of TRA when the merger is complete on June 30, 2015. Three DTRFA employees will become TRA employees and will staff a new TRA satellite office in Duluth.

The 2014 Omnibus Pensions and Retirement Bill authorized the merger of the DTRFA into TRA. The bill provides over $14 million in annual, ongoing state aid to TRA to cover the unfunded liabilities of the Duluth system and redirects approximately a half-million dollars

(Continued on page 5)

Meet Mansco Perry

Q&A with the State Board of Investment chief

When Minnesota State Board of Investment Executive Director Mansco Perry III talks about money management, invariably he'll sprinkle his conversation with baseball references or compare investments to ice cream flavors: In years past, he'll note, the choices ranged from chocolate and vanilla to strawberry, whereas today you can also get a little mocha almond, tutti-frutti or cherry raspberry in your portfolio.

But when you manage a $60 billion public retirement fund with an enviable long-term investment-return track record, you think long and hard before throwing tutti-frutti into the mix.

Perry came to SBI in 2013 from Macalester College, where he managed the school's investments. Before joining Macalester he ran the investment arm of the Maryland State Retirement Agency, and from 1990 to 2008, he worked at SBI for longtime director Howard Bicker. We sat down with "MP3" recently to talk about his first year at the helm of the Minnesota SBI.

What's your investment philosophy?

I try to be strategic rather than tactical, which really means that we focus on the long term – and when we decide what the asset allocation is, that's what we try to manage to. I try to be patient and disciplined in what we're doing. Rebalancing is a policy, so we need to keep within that asset allocation. If it goes out of balance, we try to move it back to where it is supposed to be. We have a strategy and try to follow it. There are a lot of different things to invest in out there, so we try to look at them and try to figure out what's appropriate for us. You want to understand why you're investing in something, and also understand why you don't want to. Take hedge funds. I don't know if they're good or bad, but if they're bad, I want to really understand why they're bad rather than [simply that] they're something different and foreign.

What lessons do you bring from your time in Maryland and at Macalester?

There's more than one way to build a successful mouse trap, and you

(Continued on page 4)

President's corner

Martha Lee (Marti) Zins, President

Pensions = smart money

There are certain facts about public pensions that critics of public pensions really like to ignore. One inconvenient truth: Pensions are a really good deal.

A new study from the National Institute on Retirement Security (NIRS) concludes that defined-benefit (DB) pension plans like TRA have built-in economic efficiencies that drive significant cost savings for taxpayers and government employers. According to NIRS, decision-makers should continue to carefully evaluate claims that defined-contribution (DC) or 401(k)-type plans will save money.

"Still a Better Bang for the Buck," an update of a 2008 NIRS study, looked at a model population of 1,000 female teachers who work for 30 years with a final salary of $60,000. The "target" retirement benefit for the purposes of the study was about $2,700 a month beginning at age 62. The study compared the cost to fund this benefit through both a DB plan structure and a DC plan structure. The study found:

- DB plans can deliver the same retirement benefit at about half the cost of a DC. If you compare a DB with an individually-directed DC, the DB costs are 16.3 percent of payroll compared to 31.3 percent for the DC.
- DB plans still do more with less. The per-employee lump sum amount required at age 62 to fund the target benefit is $504,732 with a DB versus the $803,236 needed in an individually-directed DC to fund the same benefit.
- The costs to fund both DB and DC pensions have risen since NIRS' 2008 study because of longer life expectancies and lower rates of investment return.

There are three significant areas in which DBs offer a better deal than DCs: longevity risk pooling, portfolio diversification, and investment fees.

Longevity risk pooling gives DB pensions a big advantage over individually-directed plans. Because they cover large numbers of retirees, DB plans can be funded to last the average life expectancy of retirees, yet pay monthly benefits to retirees as long as they live. (And teachers are a hardy breed – the average life expectancy for NIRS' sample of 1,000 retired female teachers is 90 years old!)

Because individuals must plan for significantly longer than expected life expectancy, more money must be accumulated in a DC compared to a DB. The lack of longevity risk pooling drives up the cost of DCs because individuals must "self-insure" longevity risks.

Portfolio diversification is another area in which investments are radically different under DBs as opposed to DCs. DB plans can maintain a well-diversified portfolio over time, unlike individuals who must adjust risk as they age. To protect against market shocks, individuals in DC plans are advised to shift toward more conservative investments as they age, sacrificing some expected return. Lower returns mean more money must be contributed to deliver the same level of benefits.

Lower fees and professional management are features of DB plans. Pooled investments result in lower expenses because pension fund managers can negotiate lower, large-group pricing. DC accounts incur added costs to individuals in the form of transaction fees and record keeping, and added costs to employers who must provide investment education services to employees.

Individual investors tend to underperform professionally managed DBs. Individuals also often fail to re-balance their portfolios and engage in poorly timed investment decisions. We're human, and unlike professional investors we have a tendency to react impulsively and emotionally to market swings.

When longevity risk, lower investment returns and higher fees are factored in, a DC account requires more than $800,000 for each age 62 retiree.

The study tallied up DB cost savings compared to a typical DC and found that longevity risk pooling saves 10 percent, maintenance of portfolio diversification saves 11 percent, and lower fees and professional management saves 27 percent. The total savings in DB plans comes to 48 percent.

The same benefit at almost half the cost – that's the power of being in the public fund investment pool with professional fund managers as your financial "lifeguards."

We'll stay in the pool, thanks. The water's fine.

2014 financial status: Another good year for investments

The 2014 TRA Comprehensive Annual Financial Report is now available for viewing at www.minnesotatra.org/formspub/2014annualrpt.html.

The period from July 1, 2013 to June 30, 2014, was a strong year for TRA. The assets TRA uses to pay benefits were approximately $20.29 billion, up from $18.01 billion the previous year.

Investments: Stronger than expected investment performance was the primary driver of the increase. All TRA assets are invested by the Minnesota State Board of Investment (SBI).

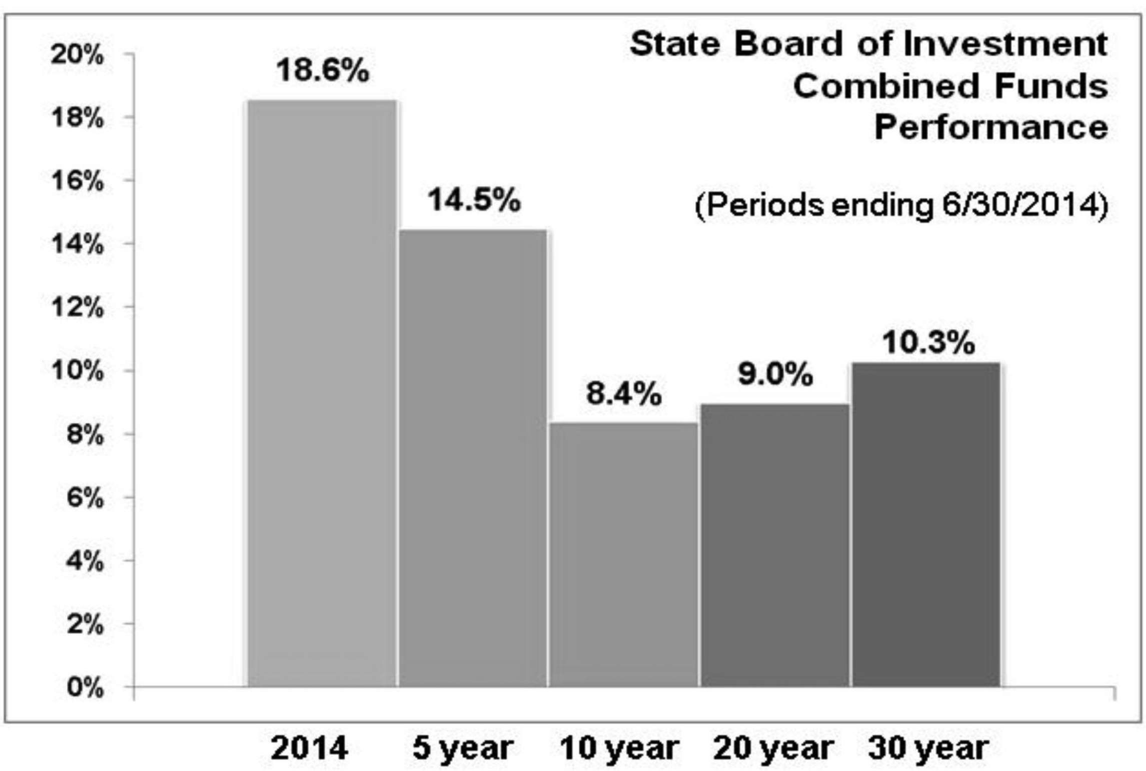
The TRA Fund posted a return of 18.6 percent during the 2014 fiscal year, compared to a 14.2 percent return the previous year. During fiscal year 2014, domestic stocks returned 25.9 percent. International stocks rose 21.4 percent for the fiscal year. The fixed income (bond) portfolio rose 5.0 percent. Alternative investments, including real estate and private equity, posted a return of 18.9 percent for the fiscal year.

Revenue: The TRA investment portfolio experienced net investment income for the fiscal year of $3.26 billion. Total employee and employer contributions were $620 million. Total net operating revenue was $3.88 billion.

Expenses: Benefit payments made during fiscal year 2014 were $1.58 billion, or about $132 million per month. During the fiscal year, $12.6 million in refunds were paid to members who left teaching and chose to withdraw their contributions plus interest. Total administrative expenses were $9.4 million. Total operating expenses were about $1.60 billion.

Funding status: When calculating funded ratios, TRA invesetment gains and losses are smoothed over five years. Using this method, TRA's funded ratio was 74.3 percent as of June 30, 2014. On June 30, the actuarial value of TRA assets was $18.2 billion and the actuarial liability (the amount needed to pay benefits) to both active and retired members was $24.5 billion, producing an unfunded liability of $6.3 billion. TRA's contribution deficiency was 3.47 percent of active-member salaries.

Using a market value of assets measure (with no smoothing of losses or gains), TRA's funded status was 82.7 percent. Under this method of assessing funding health, TRA's unfunded liability was $4.2 billion and the contribution deficiency was 0.07 percent of active member salaries.



Q&A with investment chief Mansco Perry

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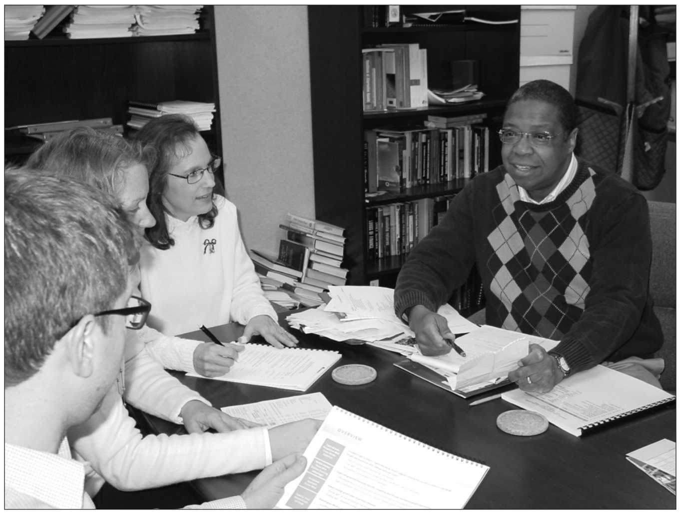
shouldn't be afraid to evaluate different approaches to things. Doesn't mean you necessarily do it, but when you're thinking about what you should do, you should look on different experiences that you had and you might find something that you've never done and it turns out to be something that we can profit by in the future. We should look at everything. We might not change a bleepety-bleep thing in the portfolio, but that doesn't mean that just because we've been successful and good that there aren't other good ideas out there. … On the other hand, I don't care if [an investment firm] has a track record of delivering 50 percent returns every year, if you can't understand what they do, you shouldn't do it.

SBI has averaged an annual return of 10.3 percent since 1980. To what do you attribute that success?

The organization has been pretty disciplined, pretty patient, had a long-term focus. We've been fortunate; we've had more good years than bad. If you narrow it down, it's pretty simple. There are really only two basic things an investor can do, in my perspective: They can own something or they can lend something. That's all we do. What's smart to own and who's smart to lend to? The smart ones to lend to are the ones you know will pay back the money you lent them, plus a reasonable return. The smart things to own are the things you can put money into and you've got some comfort that over a period of time you're going to get that money back and you're going to get a nice handsome profit. It's really as simple as that.

How does your approach differ from that of Howard Bicker?

Philosophically we're both conservative. He'll probably tell you that I'm cheap. But I'd say that maybe I'm a little bit more curious about things. Howard probably has more conviction when it comes to making a decision, and he has had an uncanny ability to just zero in on something and focus. I probably over-



Mansco Perry, right, meets with SBI staff.

analyze things and people would not be exaggerating too much if they said, 'Well, Mansco maybe goes through a few too many mental gymnastics.' But ultimately I arrive at a decision that I at least understand the logic of, and when I arrive at it, and I'm convinced, you have to convince me that what I'm doing doesn't make sense for me to kind of want to waver. Although I'm always willing to listen.

To whom do you turn for advice?

I try to develop a wide variety of networks of people I respect and believe have some intelligence and experience who maybe do the same thing I do or maybe work at some of the firms we hire. I try to get a lot of diverse perspectives on things. You can't be afraid to make mistakes, but if you do, you try to learn from them. You try to pick the brains of a lot of people you respect. … The one good thing about working for a fund as large as ours is that it gives you access to some of the brightest people in the world.

What's your opinion of defined contribution vs. defined benefit plans?

I'm a strong believer in defined benefit plans for a variety of reasons. We're trying to provide retirement income security, and you get that with both defined contribution and defined benefit but there are more opportunities to invest for higher rates of return in a defined benefit plan. There's this massive pooling effect such that generally you're professionally managing the entire portfolio whereas [with individual investors], some may know what they're doing and some may not. … Having a defined benefit plan as a base is something I believe is critical.

Defined contribution plans as a supplement to that makes a lot of sense.

Why did you choose a public-sector career?

One of Yogi Berra's famous sayings is, 'When you come to a fork in the road, take it.' I didn't start out to do this, but over my life I've come to a lot of forks in the road and the ones I took led me here, and I kind of saw that I liked it. When I woke up in the morning I had some interesting things to do. That doesn't mean I didn't think about doing other things, and I turned down a few organizations because I liked what I was doing. The last fork I took led me back here. If you're asking me what job would I pick for myself if I could, I'd be the owner of the New York Yankees and I'd be in seventh heaven, but no roads led to that.

TRA news briefs

2 percent COLA granted Jan. 1

A post-retirement increase of 2 percent went into effect on Jan. 1. Members who started receiving a benefit on or before July 1, 2013, received a 2 percent increase. Members who started receiving a benefit between July 2, 2013 and June 1, 2014, will get a prorated increase (see chart at www.minnesotatra.org/member info/r-pradjust.html).

If you are eligible for a post-retirement increase on Jan. 1, you may have already received a letter detailing the increase to your monthly benefit, along with current tax information. State and federal tax tables are available on our website under Forms and Publications.

And about those taxes...

If you set up an online account, you'll receive an e-mail when your 1099-R tax form is available online. 1099-R forms will be available online at www.minnesotatra.org before you receive your copy by mail.

Make sure your address is up to date so you get your 1099-R tax form. The form will be mailed by Jan. 31, 2015, and is needed for your 2014 tax returns.

You may initiate, renew, or revoke your current tax withholding designation at any time. If you decide to reduce or revoke the amount of income tax withheld, you will be responsible for any penalty incurred under federal tax laws if the amount withheld is inadequate.

If you move out of state permanently, notifying TRA of a change of address is not sufficient authorization for TRA to discontinue withholding Minnesota state taxes. Questions? Call 800-657-3669 or 651-296-2409.

Snowbird alert

Flying south for the winter? Don't forget to provide TRA with a temporary address. Your 1099-R tax form will go to the current address on file. Update your address on our website, www.minnesotatra.org, or call 800-657-3669 or 651-296-2409.

Set up your online account today

Make it a New Year's resolution to set up your TRA online account if you haven't yet done so!

The TRA website provides you with immediate access to the most up-to-date information about your account. To register, go to www.minnesotatra.org and click MyTRA Login. Then, click the register button and create a user ID and password.

Next you'll enter your Social Security number, choose a security question and answer, and enter your e-mail address. Your SSN or TRA number, date of birth and security question/answer will be used to verify your identity should you forget your user ID or password.

Now you can view your account information, and update your contact information, including your e-mail and physical addresses.

Duluth consolidation

(Continued from page 1)

per year in existing Duluth state aid to TRA. The boards of both TRA and DTRFA approved the merger as well as the membership of the Duluth fund.

The teacher fund consolidation continues the practice of the legislature to consolidate stand-alone funds into the statewide pension plans, when necessary, to make them sustainable.

Merging DTRFA into TRA follows past practice and precedent by protecting TRA contributing members and school districts. The legislation assures that the unfunded liabilities of the merging system are funded by ongoing state aid, safeguarding the assets of the TRA fund.

2015 Direct Deposit Schedule

January 2	July 1
February 2	August 3
March 2	September 1
April 1	October 1
May 1	November 2
June 1	December 1

Clip and Save

Teachers Retirement Association

60 Empire Drive Suite 400
St Paul Minnesota 55103-4000

800.657.3669 | 651.296.2409

www.minnesotatra.org

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Please check all boxes that apply: ☐ Name change ☐ Address change ☐ Email address addition/change

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City, State and Zip Code		Email Address	

Be careful out there...

Safeguarding your personal information from financial fraud and identity theft is more important than ever, given the high-profile data breaches that have been in the news lately.

The Federal Trade Commission has tips on protecting yourself at www.consumer.ftc.gov/articles. If you haven't been as diligent as you'd like about creating strong passwords, encrypting information online, or safely disposing of an old computer or mobile device, be vigilant.

Here are some clues that someone has stolen your information:

- Withdrawals from your bank account that you can't explain.
- You don't get your bills or other mail.
- Merchants refuse your checks.
- Debt collectors call you about debts that aren't yours.
- You find unfamiliar accounts or charges on your credit report.
- Medical providers bill you for services you didn't use.
- Your health plan rejects your legitimate claim because the records show you've reached your benefits limit.
- A health plan won't cover you because your medical records show a condition you don't have.
- IRS notifies you that more than one tax return is filed in your name or that you have income from an employer you don't work for.
- You get notice that your information was compromised by a data breach at a company where you do business or have an account.

Minnesota Teachers Retirement Association

Executive Director, Laurie Fiori Hacking

The *TRIB* is published three times a year. If differences develop between the information provided and the laws of TRA, the laws prevail.