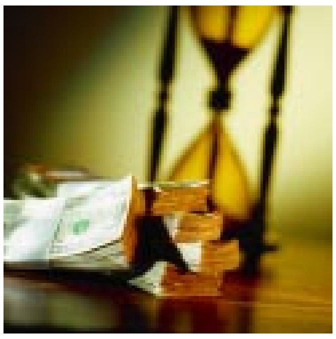


E V O L U T I O N

O F M O S E R S ' B E N E F I T S

Although the beginning of public pension plans in the United States dates as far back as 1857, the state of Missouri did not develop a system to cover its general employees until 1956. It was that year, when an ambitious and enterprising group of state employees discussed the possibility of starting a retirement plan and requested their colleagues to donate fifty cents if they were interested in participating. An actuarial firm from St. Louis was hired with the proceeds of that fund raising effort to draft legislation, which resulted in the creation of the Missouri State Employees' Retirement System (MOSERS). Since that time, MOSERS' membership has increased to nearly 90,000 active, terminated-vested, and retired participants.

MOSERS was established as a division of the Department of Revenue, under an act of the 69th General Assembly (House Bill 188). The Missouri Legislature, however, failed to appropriate any money that year for the operation of the system. Various state departments loaned MOSERS furniture and supplies in the interim and subsidized the salaries of three of the system's five employees until the legislature reconvened and appropriated money for MOSERS operation in 1958.

Benefit Improvements for General State Employees *Missouri State Employees' Plan (MSEP)*		
Benefit Provisions	1957	2000
Benefit Formula Factor (Multiplier)	.83% (.0083)	1.6% (.016)
Retirement Eligibility	Age 65 with 15 years of service Age 60 with 20 years of service	Age 65 with 5 years of service Age 60 with 15 years of service "Rule of 80" - at least age 50 with age and service equaling 80 or more
Cost-of-Living Allowance (COLA)	Not available	80% of the Consumer Price Index (CPI)
Employee Contribution Rate	4% of pay	None - contributions paid by the state
Survivor Benefit Options	Not available	*(Unreduced)* Joint & 50% Survivor Option Joint & 100% Survivor Option Life Income w/ 60 Guaranteed Payments Life Income w/ 120 Guaranteed Payments
Final Average Pay (FAP) Period	Highest 60 consecutive months	Highest 36 consecutive months
Salary Limit for Retirement	Up to $7,500 per year	No limit
Service Required for Membership	At least 1,500 hours per year	At least 1,000 hours per year

MOSERS

It is hard to visualize the changes over the years. The following illustrates key changes in benefit provisions of the MSEP prior to the establishment of the Missouri State Employees' Plan 2000 (MSEP 2000).

Benefit Multiplier

Year Enacted	Factor
1957	0.83% (.0083)
1961	1.00% (.0100)
1975	1.25% (.0125)
1979	Minimum benefit ($7.50 per year)
1984	1.33% (.0133)
1984	Uniformed members of the water patrol-base benefit increased by 1/3
1986	Minimum benefit ($12.00 per year)
1988	1.50% (.015)
1995	1.60% (.016)
	Minimum benefit ($15/year of service)

Survivor Benefit Options

Year Enacted	Optional Forms of Payment Available
1957	None
1967	Joint & 100% Survivor first made available
1982	Joint & 50% Survivor
	Life Income with 60 Guaranteed Payments
	Life Income with 120 Guaranteed Payments
1984	Unreduced Joint & 50% Survivor for Dept. of Conservation
1994	Pop-up provision for joint & survivor options
1995	Deferred Retirement Lump Sum Option (cash out)
1997	Unreduced Joint & 50% Survivor for all general state employees
1999	May re-elect joint & survivor options after retirement in certain cases

Normal Retirement Eligibility

Year Enacted	Age and Service Requirements
1957	Age 65 with 15 years of service
	Age 60 with 20 years of service
1972	Age 65 with 4 years of service
	Age 60 with 15 years of service
1986	Age 55 with 30 years of service
1992	"Rule of 80" at age 55 with temporary window
1994	Permanent "Rule of 80" at age 50 was added

Vesting

Year Enacted	Service Requirement
1957	No provision
1972	Vested with 10 years of service (if left after age 35)
1981	Vested with 10 years of service
1984	Graded vesting with 5 years of service (reduced benefits)
1992	Vested with 5 years of service

Cost-of-Living Allowances (COLAs)

Year Enacted	Annual COLA Amount
1957	None
1981	80% of the CPI with 4% minimum and 5% maximum (50% COLA cap)
1986	Cap increased to 65%
1992	Cap reset to base benefit amount in 1986
1994	COLA extended to survivors
1997	COLA extended for life beyond reaching 65% cap

Other Key Changes to the MSEP

- In 1967 the annual salary considered for retirement purposes was increased from $7,500 to $15,000. In 1972, the annual salary cap was eliminated.
- In 1972 the system became noncontributory. Through a series of changes between 1972 and 1988, member contributions were refunded. *(Most plans for state employees continue to require member contributions – the average member contribution rate in contributory systems where members are also covered by social security is 5 percent of pay, and the average benefit multiplier in those plans is 1.8% – only fractionally higher than the MOSERS' benefit multiplier.)*
- In 1981 the final average salary period was reduced from five years to three years.
- In 1984 the requirement for membership was reduced from 1,500 hours annually to 1,000 hours annually. Beyond that, between enactment and the present date, a number of provisions have been added, which allow for the subsidized purchase or transfer of credit for service outside state government.

Under the original plan, for every $1,000 in final average pay, a member retiring with 30 years of service received $249 with no COLA and no survivor benefits. Today under the MSEP, for every $1,000 in final average pay, a member retiring with 30 years of service receives $480, which includes automatic COLAs and automatic survivor benefits (if married). As you can see, the base benefit in the MSEP has almost doubled since inception of the plan and, all things considered, its value has increased by a much larger multiple. In fact, the MSEP benefits plus Social Security more than achieve the state's objective of 75% wage replacement at age 62 for the typical member retiring with 30 or more years of service, and this is provided at no cost to the employee for the MSEP benefits.

MSEP 2000

In 1998 the governor established the Public Safety Retirement Advisory Commission (PSRAC), whose primary charge was to determine which, if any, additional groups of employees should be eligible for the extra 1/3 benefit available to uniformed highway patrol and water patrol employees.

One of the first discoveries made by the PSRAC was that the extra 1/3 benefit was intended to serve as a benefit equalizer, and stemmed from the fact that different mandatory retirement ages existed for highway patrol and general employees at the time the benefit provision was enacted. The PSRAC further learned that in the case of general employees the mandatory retirement age has since been eliminated, and the mandatory retirement age for patrol employees has since been extended five years. Consequently, there no longer appeared to even be a rational basis for the present differential, so the notion that it might be extended to other groups received very little consideration. (The PSRAC did, however, take note of the fact that employees in public safety positions tend to go to work for the state at relatively young ages and make careers of those positions.)

Armed with this information, the PSRAC set about the task of designing a new retirement system for future hires, which would align retirement plan provisions with the state's personnel management objectives and achieve at least the following objectives:

- Allow career employees (meaning employees with 30 or more years of service) to retire with retirement income approximating 75% of pre-retirement gross income, regardless of age at retirement.
- Provide meaningful levels of survivor benefits in duty-related death cases, regardless of employee classification.
- Eliminate inequities, which have crept into the existing plan.
- Encourage new hires to make careers of state service.
- Do all of the above without impacting the cost of the retirement plan.

In order to maintain the same level of cost as the existing plan and achieve the objectives identified, it was clear there would need to be tradeoffs between the existing plan's benefits and the benefits to be provided by the new plan. Consequently, employees who were participants in the old plan could not automatically be placed in the new plan. (That is, it could not automatically be assumed they would wish to give up certain features of the old plan.)

The objective was to rearrange benefits for future hires in such a way that stated personnel objectives would be achieved within the cost parameters of the old plan. However, it was also realized that some employees and retirees would likely prefer to participate in the new plan. Accordingly, even though increasing benefits for present plan participants was not an objective of the new plan design, provisions were included to allow active and retired participants in the old plan to switch to the new plan on a voluntary basis if they so desired.

Risk

Regardless of the type of retirement arrangement in place, there are a number of risk areas which must be addressed, such as:

- At what age will people retire?
- How many people will terminate before being eligible for benefits?
- How long will people live after retirement?
- What kind of salary increases will people receive?
- How much income will be produced by invested assets?

With a defined benefit plan, such as MOSERS, all of these risks are borne by the employer. That is, unfavorable experience in any of these areas increases the cost for the state. A general principle of any type of risk related activity is that the party assuming the risk of adverse experience is the same party who will be the beneficiary of favorable experience. In contrast to this general principle, the state has used the proceeds of favorable experience (particularly the favorable investment experience of the last two decades) to increase retirement benefits for employees.

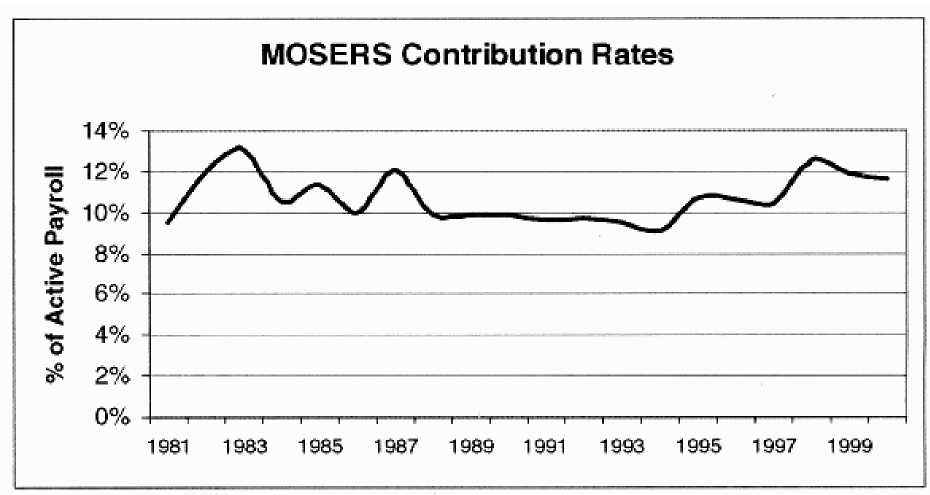
Contribution Rates

You do not contribute toward your retirement benefit. Since September 1, 1972, retirement benefits have been financed solely by state contributions and investment earnings on those contributions. Each October, MOSERS' Board of Trustees establishes a contribution rate for the next fiscal year. The contribution rate, which is set as a percentage of payroll, is actuarially calculated to cover the system's benefit obligations and administrative costs for the coming fiscal year and the future. When the system's actuary calculates the contribution rate, it is based on a number of factors including the current level of benefits, how many members are in the plan, current and expected future pay levels, the age, service, and life expectancy of members, expected earnings on investments, and the plan's unfunded liability.

Conclusion

The retirement plan has generated substantial experience gains over the years, primarily as the result of very favorable investment markets. The state, as the risk bearer, had the option of either taking those gains and using them for other purposes, such as reducing the contribution rate, or using those gains to increase benefit levels. The state chose to increase benefit levels. Perhaps the best indicator of that is the state's contribution rate history over the last 20 years, which is illustrated in the chart below. In the absence of the benefit increases mentioned, it is almost certain the state's contribution rate for retirement benefits would have by now been reduced to zero.

A prolonged bull market (like the one we have been experiencing for almost 20 years) tends to build expectations about future performance. While it is impossible to predict the direction or magnitude of likely future financial market changes (particularly in the short term), it is clear that present high market valuations are going to make it increasingly difficult to sustain the rates of return seen in the recent past. Consequently, it is unlikely that the system will be able to produce the kinds of experience gains seen in the past two decades. It should, however, be possible to maintain the state's contribution rate at approximately its present level, absent any significant future increases in retirement benefits.



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