

Legislative Commission on Pensions and Retirement

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TO: Members of the Legislative Commission on Pensions and Retirement

FROM: Chad Burkitt, Analyst

DATE: March 22, 2019

RE: H.F. 2671 (Nelson); S.F. 243 (Frentz): Minnesota State Higher Education Individual Retirement Account Plan; Increasing employer contributions

Introduction and Background

H.F. 2671 (Nelson); S.F. 243 (Frentz), phases in an increase in the employer contribution rate for the Individual Retirement Account Plan (IRAP) from the current 6% to 8.75% by 2024.

Author's Amendment H2671-1A ties the IRAP employer contribution rate to the employee contribution rate for the Teachers Retirement Association (TRA). The amendment further reduces the phase-in rate so that the contribution rate increases by 0.35% each year between fiscal year 2020 and fiscal year 2025. Therefore, the contribution rates proposed by the amendment for the IRAP would be as follows:

<u>Fiscal Year</u>	<u>Proposed Contribution Rate</u>
2019 (Current Rate)	6%
2020	6.35%
2021	6.7%
2022	7.0%
2023	7.4%
2024	7.75
2025	TRA employee contribution rate

This bill should be considered in the context of the employee contribution increase required by H.F. 2489 (Murphy, by request), which increases employee contribution rates to the TRA employee contribution rate. If H.F. 2489 is enacted, then under the amended H.F. 2671 (Nelson); S.F. 243 (Frentz), the IRAP employer and IRAP employee contribution rates would match.

The current employer contribution rate of 6% has been in place since the plan was established in 1988. The rate of 6% appears to have been selected to conform with the Unclassified Employees Retirement Program of the Minnesota State Retirement System (MSRS Unclassified Plan). The 2018 Omnibus Retirement Bill increased the Unclassified Plan's contribution rate from 6 percent to 6.25% effective July 1, 2019. With this change, the employer contribution rate for the Unclassified Plan matches the employer contribution rate of the MSRS General State Employees Retirement Plan (MSRS General).

Discussion and Analysis

1. Recruitment and retention. One possible policy objective for an employer contribution increase is improved recruitment and retention of employees. To do this, Minnesota State must provide a package of benefits including retirement benefits that are competitive within a regional and, sometimes national market. An informal survey of surrounding higher education systems provides the following data:

<u>Higher Education System</u>	<u>Primary Ret. Plan Type</u>	<u>Employee Contribution</u>	<u>Employer Contribution</u>
<i>Minnesota State</i>	<i>Mandatory participation defined contribution plan (with option to elect defined benefit)</i>	<i>4.5% (current rate)</i>	<i>6% (current rate)</i>
University of Minnesota	Mandatory participation defined contribution plan	5.5%	10% (13% hired before 1/2/2012)
University of Wisconsin Colleges	Mandatory participation defined benefit plan	6.5%	6.5%
Wisconsin Technical College System	Mandatory participation defined benefit plan	6.5%	6.5%
University of Iowa and Iowa State Colleges and Universities	Mandatory participation defined contribution plan (with option to elect defined benefit)	5%	10%
South Dakota Public Universities	Mandatory participation defined benefit plan	6%	6%
North Dakota University System	Mandatory participation defined contribution plan	4.5%	12.5%

For ease of presentation, the above table does not describe various complexities, such as tiered benefit systems, or scheduled rate changes.

2. Employer vs. employee contribution rates. If H.F. 2489 (Murphy, by request) becomes law, then the IRAP employee contribution rate will be greater than the employer contribution rate. It is typical for public retirement plans to have an employee contribution rate that is less than or equal to its employer contribution rate.
3. Cost. Increasing the employer contribution rate for the IRAP will incur a cost to Minnesota State. According to Minnesota State, the IRAP’s 2018 covered payroll was \$502,417,715. The bill provides for a first year increase of 0.35% of covered payroll equal to \$1,758,462. The total increase of 2.75% of covered payroll is equal to \$8,792,310. Since these figures do not account for payroll growth, they likely understate the actual cost.

4. Employer contributions to the IRAP vs. employer contributions to TRA. The bill, as introduced, would have increased the employer contributions from 6% to 8.75% in 0.55% increments, which would have made the contribution rate equal to the TRA contribution rate in FY 2024. (Under the 2018 omnibus pension bill, TRA's employer contributions increase every year in .21% increments, until they reach 8.75% in FY 2024.)

In theory, an argument could be made for making the employer contributions to the two plans equal. Why shouldn't Minnesota State have to contribute the same amount, regardless of whether the member elects to be covered by TRA rather than the IRAP?

The response would be that the two plans are different types of plans—the IRAP is a defined contribution plan and TRA is a defined benefit plan. When a dollar of employer contribution is paid into the IRAP, it is directly deposited into an account in the member's name and thus directly benefits the member. However, of the 17.18% of covered payroll that is the 2018 actuarially determined contribution to TRA, 7.7% of payroll goes to pay off unfunded liabilities. Put another way, 45 cents of each dollar contributed to TRA is being used to pay off the unfunded liabilities that have accrued over years of contributing less than is required to fund annual accruals. In other words, the employer contribution to TRA pays for more than just a single employee's benefit.

The value of the benefit being purchased under these plans may be the more valid comparison, not the amount of the contributions being made for the benefits.

1.1 moves to amend H.F. No. 2671; S.F. No. 243, as follows:

1.2 Page 1, line 9, delete "6.55" and insert "6.35" and delete "7.1" and insert "6.7" and delete
1.3 "7.65" and insert "7.05"

1.4 Page 1, line 10, delete "8.2" and insert "7.4" and delete "8.75" and insert "7.75" and
1.5 delete "and later" and before the period insert ". Starting in fiscal year 2025, the employer
1.6 contribution rate is equal to the coordinated employee contribution rate in section 354.42,
1.7 subdivision 2"

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State of Minnesota

HOUSE OF REPRESENTATIVES

NINETY-FIRST SESSION

H. F. No. **2671**

03/21/2019 Authored by Nelson
The bill was read for the first time and referred to the Committee on Ways and Means

1.1 A bill for an act
1.2 relating to retirement; increasing contribution rate for the higher education
1.3 individual retirement account plan; amending Minnesota Statutes 2018, section
1.4 354B.23, subdivision 3.

1.5 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF MINNESOTA:

1.6 Section 1. Minnesota Statutes 2018, section 354B.23, subdivision 3, is amended to read:

1.7 Subd. 3. **Employer contribution rate.** The employer contribution rate on behalf of
1.8 participants in the individual retirement account plan is six percent of salary in fiscal year
1.9 2019, 6.55 percent in fiscal year 2020, 7.1 percent in fiscal year 2021, 7.65 percent in fiscal
1.10 year 2022, 8.2 percent in fiscal year 2023, and 8.75 percent in fiscal year 2024 and later.

1.11 **EFFECTIVE DATE.** This section is effective the day following final enactment.