HF 4081 (Stephenson); SF 4092 (Gustafson): PERA Local Government Correctional Service Retirement Plan; Increasing the multiplier used to calculate the annuity amount, increasing the employee and employer contribution rate

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Introduction

Affected Plan(s): Public Employees Retirement Association (PERA) Local Government Correctional Service Retirement Plan (PERA Correctional)

Laws Amended: Minnesota Statutes, sections 353E.03 and 343E.04

Brief Description: The bill increases the multiplier used to calculate the annuity amount for members of PERA Correctional from 1.9 percent to 2.2 percent of the employee's average salary. The new multiplier applies to years of service earned after June 30, 2024. The benefit improvement is paid for by an increase in employee and employer contributions.

Attachment: Memo from PERA staff to the PERA Board of Trustees dated March 14, 2024

Background

When a member of a public pension plan in Minnesota retires, the member's lifetime benefit is calculated using a formula defined in statute. The benefit formula used to calculate a retirement annuity from PERA Correctional is based on three components:[1]

1. years of allowable service, which is the number of years working in a job with PERA Correctional coverage;
2. multiplier, sometimes called an accrual rate, which is currently 1.9 percent for PERA Correctional; and
3. high-five average salary, which is the average gross salary during a member's five highest-paid consecutive years of credited service.

[1] Minn. Stat. §353E.04, subdivision 3.

These three components are multiplied together to equal a member's annual benefit amount, as shown below:

Annual benefit = Years of service x Multiplier x High-five average annual salary

The bill increases the multiplier for the PERA Correctional from 1.9 percent to 2.2 percent prospectively. This benefit improvement is paid for by an increase in employee and employer contributions.

Section- by- Section Summary

Section 1 amends section 353E.03, subdivisions 1 and 2, by increasing the employee and employer contribution rate, respectively. Section 1 increases the employee contribution rate by one percent of pay, from 5.83 percent to 6.83 percent, and the employer contribution rate by 1.5 percent of pay, from 8.75 percent to 10.25 percent. The section is effective beginning with the first full pay period after July 1, 2024.

Section 2 amends section 353E.04, subdivision 3, by increasing the multiplier used to calculate the annuity amount from 1.9 percent of pay to 2.2 percent.

The multiplier of 2.2 percent applies to years of service earned after June 30, 2024, which is the effective date of section 2. Service earned prior to the effective date will still be based on the multiplier of 1.9 percent. As a result, the benefit formula proposed by the bill is:

Annual benefit = ((Years of service earned prior to July 1, 2024 x 1.9 percent)
+ (Years of service earned after June 30, 2024 x 2.2 percent)) x High-five average annual salary

Public Policy Considerations

Cost

According to a memo from PERA staff to the PERA Board of Trustees dated March 14, 2024, PERA's retained actuary calculated the cost of the bill. The estimated cost for the benefit improvement is 2.5 percent of pay. Since the bill increases contributions by a total of 2.5 percent of pay, the contribution increase is sufficient to pay for the increase in liability. Related to the methodology for the calculation, the PERA memo states the following:

> *The cost for the existing members varies depending on the amortization period used to spread the unfunded liability. Under the cost methodology required to be used to determine contribution requirements (the Entry Age Normal Cost Method), there is a component of cost determined as a past service liability even though the multiplier is effective for future service. Staff recommends that the amortization period for payment of the unfunded liability be set at 10 years, which is approximately the average expected remaining working lifetime for the initial transfer group.*

Multiplier Comparison

It is common in Minnesota for public pension plans with a similar membership to have the same multiplier. The PERA General Plan and the Minnesota State Retirement System (MSRS) General Plan both have a multiplier of 1.7 percent. The state's two teacher pension plans, the Teachers Retirement Association and the St. Paul Teachers' Retirement Fund Association, both have a multiplier of 1.9 percent. The state's two public safety plans, the PERA Police and Fire Plan and the MSRS State Patrol Plan, both have a multiplier of three percent.

PERA Correctional was established in 1999. Since that time, the plan's multiplier has been 1.9 percent.[2] The multiplier for the MSRS State Correctional Employees Retirement Plan (MSRS Correctional) is 2.2 percent for employees hired on or after July 1, 2010, and 2.4 percent for members hired prior to July 1, 2010. The bill would bring the multiplier for PERA Correctional into alignment with MSRS Correctional for newly hired employees.

While it is common for plans with a similar membership to have the same multiplier, it is not always the case. PERA Correctional and MSRS Correctional have significantly different contribution rates, which is an important factor that affects the design of each plan. PERA Correctional currently has an employee and employer contribution rate of 5.83 percent and 8.75 percent, respectively, which will increase under the bill, as described above. MSRS Correctional has an employee and employer contribution rate of 9.6 percent and 18.85 percent, respectively.

Impact of benefit improvement on annuity amount

Younger employees will benefit more from this proposal than older employees, because the younger employees will have earned more years of service under the higher multiplier by the time the employee retires. However, the younger employees will help pay for the benefit improvement over a longer period of time.

The chart below shows the impact of the bill on an estimated annuity amount for three hypothetical employees compared to the current benefit formula. The chart estimates a projected benefit level for a newly hired, mid-career, and late career employee. The chart assumes that each employee was or will be hired at age 25, will elect a single life annuity at retirement, and will work in a job with PERA Correctional coverage until the employee retires at age 55, the normal retirement age for PERA Correctional.

[2] Minn. Stat. §356.19, subdivision 5a (1999).

Impact of HF4081/SF4092 on the annuity amount for career employees based on hire date

	Hire date	Age in 2024	Years of service pre-2024	Years of service post-2024	Benefit accrued pre-2024	Benefit accrued post-2024	High-five Salary[3]	Total Annual Benefit
Current Benefit Formula	N/A	N/A	30	0	$42,750	$0	$75,000	$42,750
Newly hired employee	7/1/2024	25	0	30	$0	$49,500	$75,000	$49,500
Mid-Career employee	7/1/2009	40	15	15	$21,375	$24,750	$75,000	$46,125
Late Career employee	7/1/1999	50	25	5	$35,625	$8,250	$75,000	$43,875

HF4081-SF4092 Summary.docx

[3] The average salary for an active member aged 55 to 59 was $79,626 according to the PERA Correctional actuarial valuation as of June 30, 2023. The chart uses a lower salary because the high-five salary is the average gross salary during the employee's five highest-paid consecutive years of credited service. It is likely that the average high-five salary for the newly hired and mid-career employee will be higher than $75,000, due to future pay increases. However, the high-five salary is consistent in the chart to demonstrate the impact of the change in multiplier proposed by the bill.