Comparison of Retirement Benefits for Minnesota Teachers

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Public retirement plan stakeholders and their objectives

Each stakeholder group has its own objectives

- **Public employees**
  - Competitive compensation and retirement security
- **Public employers**
  - Ability to attract and retain, and an orderly turnover of workers
- **Taxpayers and recipients of public services**
  - Public services delivered in a cost-effective manner

Retirement plan design

- Sound retirement plan policy balances stakeholder objectives, which can conflict with or complement one another.

  For example:

  - Encouraging worker mobility vs. retention of experienced personnel
  - Risk-sharing can distribute effects of risk more evenly between stakeholder groups

- Plan design affects policy outcomes
  - Vesting and benefit eligibility requirements
  - Benefit levels
  - Inflation protection
  - Contribution requirements

Observations on Comparing Retirement Plan Designs

- A retirement benefit is based on multiple factors and variables
- Fairly assessing the adequacy and efficacy of a pension plan design is nuanced, complex, and defies simple ranking
- Focusing on a single factor or subset of factors, and excluding other factors, can lead to inaccurate or misleading conclusions about the efficacy of the plan design
- The full context of the plan design, including vesting periods, multipliers, eligibility criteria, salaries, COLAs, contribution rates, actuarial assumptions, and other variables must be considered when making such comparisons.
- The retirement benefit is one component, along with salary and other benefits, of the total employee compensation package
  - Just like pensions salaries and other benefits differ across states

Observations on Comparing Retirement Plan Designs

- A career teacher in Minnesota who works until age 66 (65 effective 7/1/25) receives a retirement benefit that is comparable with their counterparts in other states.
- Minnesota's normal (full) retirement age of 66 (65) is among the highest required retirement ages in the nation
- Teachers in most other states have options to retire with a full retirement benefit sooner than 66 (65).
- In some early retirement scenarios, Minnesota teachers receive a benefit that is lower as a percentage of the full retirement benefit than teachers in other states.
- But, Minnesota teachers vest sooner and qualify for a benefit at an earlier age than their counterparts in many states
- Teachers in Minnesota contribute more than teachers in other states for a similar retirement benefit.

Core elements of defined benefit plans

- NASRA maintains a dataset of plan design elements for public pension plans in every state
- Calculating pension benefits

  Years of service x Final average salary x Multiplier

- Core factors that determine the level of pension benefits include:
  - Vesting period
  - Multiplier
  - Final average salary period
  - Retirement eligibility provisions
  - COLA

Vesting period

- The level of service required to qualify for a future pension benefit
- Vesting periods range from 3 years to 10 years, with 5 years being the most common
- With a vesting period of three years, Minnesota TRA is below the national and regional average
- This allows Minnesota teachers to qualify for a future benefit sooner than teachers in other states

Multiplier

- The percentage of final average salary for each year of service accrued
- Multipliers for Social-Security eligible plans range from 1.0 percent (generally associated with hybrid plans) to as much as 2.35 percent
- Some plans use a graded multiplier, with a higher percentage of final average salary replaced for those who accrue higher levels of service credit
- With a multiplier of 1.9%, Minnesota TRA is consistent with the national and regional average

Final average salary period

- Definition: The period of compensation that the pension benefit is based on
- With a highest 5-year final average salary period, Minnesota TRA is consistent with the national and regional average
- There are other important elements to determining pensionable compensation, including limitations on the use of overtime or bonus pay in the FAS determination, or limitations on the recognition of outsized salary increases in the FAS calculation (aka “spiking”)

Normal retirement eligibility

- Definition: The age and/or level of service that must be attained to qualify to begin receiving an unreduced pension benefit
- There can be several variations of normal retirement eligibility depending on the plan. For example:
  - Different normal retirement ages corresponding to different service levels
  - “Rule of” normal retirement eligibility, such as Rule of 90 (i.e., age and service must add to 90)
  - Normal retirement eligibility at any age with a specified level of service
- How does Minnesota TRA compare?
  - Only 15 other states have only one, age-based provision for normal, unreduced retirement
  - 4 at age 62, 1 at age 63, 6 at age 65 (including MN as of 7/1/25), and 4 at age 67
  - At age 65 Minnesota is not an outlier in this regard, but most other states offer multiple paths to a full, unreduced benefit at a younger age with a greater service accrual

Early retirement eligibility

- Definition: The age and/or level of service that must be attained to qualify to begin receiving an actuarially reduced pension benefit
  - The magnitude of the actuarial reduction for early retirement varies among plans, and sometimes by age and service level within the same plan
- How does Minnesota TRA compare?
  - Minnesota TRA participants are eligible to retire with an actuarially reduced benefit as early as age 55 with only three years of service
  - In several other states teachers must accrue more service or attain a higher age to retire with a reduced benefit

Actuarial reductions for early retirement

- Definition: The percentage decrease from the normal retirement benefit that is applied to a participant's benefit when they retire before attaining normal retirement eligibility.
- How does Minnesota TRA compare?
  - The actuarial reduction factors for MN TRA – 7%/year from NRA to age 59, plus 4%/year from age 58-55 – are on the higher side
  - The actuarial reduction factors for MN TRA are not the highest we observe:
    - Indiana TRS reduces benefits by 11% per year, plus an additional 5% for each year below age 59
    - North Dakota PERS reduces benefits by 8% per year from the earlier of age 65 or attainment of Rule of 90
    - Utah RS reduces benefits by approximately 9% per year between ages 64 and 65, and 7% per year between ages 60-63

Actuarial reductions, cont.

- How does Minnesota TRA compare?
  - Most other plans, including those with greater actuarial reductions, have lower normal retirement ages or multiple paths to attaining normal retirement eligibility which can protect at least some participants from experiencing the full impact of reductions
  - The reduction in NRA from 66 to 65, which will be implemented on 7/1/25, will lessen the impact of the actuarial reduction on MN teachers who retire early by subjecting them to one fewer year of benefit reduction

Cost-of-living adjustment

- An increase to the pension benefit to offset the effect of inflation
- Some plans do not provide an automatic COLA
- Minnesota TRA:
  - automatic, 1.0%, rising gradually to 1.5% by FY 28
- The Minnesota TRA COLA is consistent with national COLA formulas

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Importance of tradeoffs, complete perspective, etc.

- It is possible to review and compare the individual elements that comprise a pension plan's design
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- It is possible to review and compare the individual elements that comprise a pension plan's design
- But to compare these elements in isolation would result in a diminished perspective about other factors present in the plan design that also affect participant outcomes
- This may also make one plan look comparatively favorable to another, in a way that it would not if all elements were considered

Importance of tradeoffs, complete perspective, etc.

- For example
  - Teachers in Michigan can retire with a full unreduced benefit at 60/10 or 55/30, but they participate in a hybrid plan with a lower multiplier and a substantial portion of their retirement income exposed to investment, longevity, and inflation risk
  - Teachers in North Dakota can retire with a full unreduced benefit at Rule of 90, but their benefit receives no guaranteed inflation protection AND those retiring before attaining Rule of 90 must take an 8% reduction to their benefit for each year below age 65 or attainment of Rule of 90

Importance of tradeoffs, complete perspective, etc.

- Examples cont.
  - South Dakota teachers who retire early experience lower actuarial reductions for early retirement, but with a higher NRA of 67 they may see greater cumulative reductions the further they are from age 67; also, they may not receive a COLA, even during periods when inflation is higher
  - Career teachers (30 YoS) in Wisconsin can retire with full benefits at age 57, but their benefit is based on a lower multiplier, and their benefit increases can be variable, including clawing back previously awarded increases, for the duration of their retirement
- Final point: we maintain this information on a comprehensive basis and we would be happy to work with the Commission staff to inform this discussion through appropriately contextualized comparatives

Spending on Public Pensions

- NASRA research shows that around 5.0 percent of all spending by states and local governments is spent on public pensions
- Minnesota spends 2.4 percent
- Does this mean Minnesota, by definition, has lower retirement benefits?
- No; many factors affect public pension spending levels
- Benefit levels are only one factor