Minnesota Statutes Chapter 353F defines terms for member benefits and reporting requirements related to entities that privatize. A privatizing entity can seek augmentation of benefits for eligible members by requesting an actuarial study measuring the impact to the General Employees Retirement Plan (the Plan). If the actuarial calculation results in a net gain to the Plan, benefits are augmented at the rate of 2 percent. If a 2 percent augmentation results in a net loss, the augmentation rate is reduced to 1 percent. If a net loss occurs at the 1 percent augmentation rate, there is no augmentation of benefits.

The actuarial test's focus centers on a comparison of two different actuarial measurements at one point in time and considers only a subset of members from that particular entity. There are three issues with the structure of this test:

1. The test ignores the fact that the Plan is currently underfunded. The result is an increase in benefits despite previously earned benefits not yet being funded. Important to note is that augmentation has been eliminated for all non-privatized members in an effort to improve the Plan's funding status.

2. The test ignores the non-active members from that entity. Retirees or previously terminated employees with benefits are essentially assumed to be fully funded when in reality, the Plan is only about 80 percent funded.

3. The test does not consider the loss of future contributions from the entity. If the loss of future contribution exceeds the gain from lower future benefit accruals, the Plan will be worse off after the entity privatizes.

The structure of the current test produces a result that does not accurately reflect the impact to the Plan. As a result, the current test is designed to be difficult to fail. The result of the current testing approach is that each privatization results in members of the privatized entity receiving 2% augmentation at the same time that the funding position of the Plan is weakened.

The actuarial test should consider more than just the difference in two actuarial measurements. The test should also consider (1) the current funding status of the Plan, (2) the existence of retired and previously terminated members from that entity, and (3) the change in future benefit accruals and contributions.

Further explanation and a real life example will be provided at the board meeting. Staff intends to ask the Board to consider the policy of privatization and changes to privatization statutes at the October board meeting.
Privatization Actuarial Test for Augmentation Eligibility
Liability estimates can be based on future service and future salaries (PV of Benefits), past service and past salaries (PV of Accrued Benefits), or a measurement that includes future salaries and service, but then allocates part of the total to past service (Actuarial Accrued Liability).
If the PV of Accrued Benefits with 2% augmentation is less than the Actuarial Accrued Liability (AAL), the Plan is said to have a net actuarial gain and 2% augmentation will be granted. However, this test does not consider the Plan’s funding status, retiree liabilities, or the impact of no future contributions.
The Plan is currently 79.5% funded (Assets/AAL). After assets are first attributed to fully fund all retired and terminated members, the remaining assets cover 44% of the total active AAL. The assets allocated to this entity to fund active member benefits would be $28.8M (44% of $65.4). Assets allocated to this entity are insufficient to fully fund retiree benefits and provide augmentation to active members.
The reduction in future contributions ($45.5M) is significant and more than offsets the gain resulting from the elimination of future benefit accruals ($22.8M). These results are not considered in the current test. After consideration of all components, the Plan is in a worse funding position after privatization (with or without augmentation).