HF 4666 (Wolgamott); SF 4878 (Frentz): Public Employees Police and Fire Retirement Plan; Increasing the Postretirement Adjustment and Decreasing the Waiting Period for a Postretirement Adjustment

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Introduction

Affected Plan(s): Public Employees Police and Fire Retirement Plan (PERA P&F)

Laws Amended: Minnesota Statutes, section 356.415, subdivision 1c

Brief Description: The bill changes the method for calculating postretirement adjustments under PERA P&F from a fixed rate adjustment of 1% to a variable rate adjustment that is linked to the postretirement adjustment for Social Security benefits with a minimum of 1% and a maximum of 1.5%. The bill also decreases the waiting period to be eligible for a full postretirement adjustment from 36 months to 12 months. The bill aligns postretirement adjustments under PERA P&F with postretirement adjustments under PERA General.

Attachment: Letter from Doug Anderson, Executive Director of the Public Employees Retirement Association (PERA), to the Commission dated March 21, 2024

Background

Minnesota's public pension plans provide annual postretirement adjustments or cost-of-living adjustments (COLAs) to retirees, which are intended to protect a retiree's pension benefit from inflation. PERA P&F currently pays a postretirement adjustment of 1% to eligible retirees and benefit recipients, which is tied for the lowest postretirement adjustment rate among Minnesota's public pension plans.

PERA P&F is a "basic" plan in which the participating members and employers do not pay into Social Security through a member's covered employment. As a result, the member's employment is not counted when determining any Social Security benefit to which the member may be entitled due to other employment. The participating members and employers of "coordinated plans," such as the PERA General Employees Retirement Plan (PERA General), contribute to Social Security and the members earn credit toward a Social Security benefit.

According to a report published by the Commission in December 2020 on a study of postretirement adjustments, members of basic plans, such as PERA P&F, are more likely to be vulnerable to inflation, because the members do not participate in Social Security through the member's covered employment.[1] Coordinated members, on the other hand, receive a COLA on the member's Social Security benefit, which is tied to an inflation measure (or index), CPI-W.[2] According to the study, "basic members receive smaller increases over time than coordinated members because of the COLAs on their Social Security benefit."[3]

How long a member expects to receive retirement benefits may impact how vulnerable a member's benefit is to inflation. Minnesota's public safety plans, including PERA P&F, have a normal retirement age of 55, which is earlier than the normal retirement age for Minnesota's general plans. For example, PERA General has a normal retirement age of 66 for most active members. A member of PERA P&F may be more vulnerable to inflation than a member of PERA General because a member of PERA P&F is expected to collect a benefit as much as 11 years earlier than a member of PERA General.

The bill aligns the postretirement adjustment under PERA P&F with the postretirement adjustments under PERA General and is likely to provide more inflation protection to PERA P&F retirees and benefit recipients than what is provided under current law.

General Summary

Summary of current law

The bill amends section 356.415, subdivision 1c, which governs postretirement adjustments for PERA P&F. Under current law, retirees of PERA P&F are eligible for an annual 1% COLA after a waiting period. Retirees are first eligible for a partial COLA after 25 months of receiving annuity payments and are eligible for the full COLA after 36 months of receiving annuity payments. The COLA is effective as of January 1 and the number of monthly payments is determined as of the preceding June 30. The partial COLA is 1/12 of 1% for each month the member was receiving payment during the year the benefit was effective, as of June 30.

For example, under current law, if a PERA P&F member retires in March 2025, the member will be eligible for a partial COLA effective January 1, 2028. The partial COLA will be one third of the full COLA or 0.33%, because the member received 4 monthly payments as of June 30, 2025. The member will be eligible for the full, 1% COLA effective January 1, 2029, and every January 1 thereafter. Individuals receiving disability or survivor benefits are also eligible for a COLA, subject to the same waiting period.

Summary of HF4666/SF4878

The bill makes two changes, which align postretirement adjustments under PERA P&F with postretirement adjustments under PERA General. The first change is that the bill uses a new method for determining postretirement adjustments for PERA P&F. Under the bill, the COLA for PERA P&F is 1%

[1] Legislative Commission on Pensions and Retirement, (2020, December), *Report on the LCPR Study of Postretirement Adjustments (COLAs).* Referred to as "LCPR COLA Study."

[2] Consumer Price Index for Urban Wage Earners and Clerical Workers

[3] LCPR COLA Study, page 35.

unless the Social Security COLA is greater than 2%, in which case the COLA is 50% of the Social Security COLA, not to exceed 1.5%.

The second change is that the waiting period for a retiree or benefit recipient to receive a full COLA is reduced from 36 months to 12 months. In addition, the waiting period for a partial COLA is reduced from 25 months to 1 month. The partial COLA is determined by the following formula:

> *Partial COLA = COLA * (the number of payments received in the preceding calendar year, as of June 30 / 12).*

For example, under the new waiting period, if a PERA P&F member retires and begins to receive annuity payments in March 2025, the member will be eligible for a partial COLA effective January 1, 2026. Since the member received payments for 4 months, as of June 30, 2025, the member will be eligible for one third of the COLA amount for that year, which will range from 0.33% to 0.5% (COLA * (4 monthly payments/12)), depending on the variable COLA. The member will be eligible for the full COLA effective January 1, 2027, and every January 1 thereafter.

The bill has one section and is effective for postretirement adjustments beginning on or after January 1, 2025.

Public Policy Considerations

Cost

Doug Anderson, Executive Director of PERA, in a letter to the Commission dated March 21, 2024, stated the following about the cost of the bill:

> *Combined the two initiatives [increasing the COLA and decreasing the waiting period] have an annual cost starting at $40 million. Full funding of these benefits means continuation of the annual funding for a 30-year period with amounts increasing as a percentage of payroll. The initial annual amount of $40 million would increase to an expected amount of $94 million in the final year of the amortization period.*

Impact of HF4666/SF4878 on annuity amount

The increased COLA and the decreased waiting period, under the bill, will increase a member's annuity benefit. The chart below compares the annual benefit increases under the current COLA, and the minimum and maximum COLA under the bill. The chart reflects the reduced waiting period and assumes that a member covered by PERA P&F will retire and start to receive a hypothetical monthly annuity benefit of $1,000 in March 2025. While the chart illustrates the minimum and maximum COLA under the bill, the COLA is likely to fluctuate from year to year.

Impact of HF4666/SF4878 on annuity amount for a retiree starting to receive payments in March 2025

Period	Current COLA	Monthly Benefit (Current COLA)	New COLA, if 1%	Monthly Benefit (1% COLA)	New COLA, if 1.5%	Monthly Benefit (1.5% COLA)
March-December 2025	0%	$1,000	0%	$1,000	0%	$1,000
January-December 2026	0%	$1,000	0.33%	$1,003.33	0.5%	$1,005.00
January-December 2027	0%	$1,000	1%	$1,013.37	1.5%	$1,020.08
January-December 2028	0.33%	$1,003.33	1%	$1,023.50	1.5%	$1,035.38
January-December 2029	1%	$1,013.37	1%	$1,033.74	1.5%	$1,050.91

Fixed vs. Variable COLA

The 2018 Omnibus Pension Bill modified the provisions for postretirement adjustments for PERA General and PERA Correctional to move away from a fixed rate adjustment to a variable rate adjustment that is tied to the COLA for Social Security benefits. The COLA for PERA General changed from a fixed rate adjustment of 1% to a variable rate adjustment with a minimum of 1% and a maximum of 1.5%. The COLA for PERA Correctional changed from a fixed rate adjustment of 2.5% to a variable rate adjustment with a minimum of 1% and a maximum of 2.5%.

The LCPR COLA Study evaluated the effect of the 2018 COLA changes on PERA General and PERA Correctional. According to the study, the new COLA model provides slightly better inflation protection for PERA General and slightly worse inflation protection for PERA Correctional. However, the change in percentages for each plan has a larger impact on the amount of inflation protection than the differences between fixed rates and variable rates. The study states:[4]

> *Ultimately, the absolute amount of the postretirement increase has a much larger effect on the degree of inflation protection than whether or not the calculation method for calculating the increase is linked to inflation, particularly when caps are used to limit the total amount that can be paid.*

[4] LCPR COLA Study, page 37.

It is likely that the method for determining postretirement adjustments under the bill will provide more inflation protection to PERA P&F retirees and benefit recipients than the current fixed rate adjustment of 1%.

Under the bill, the variable COLA for PERA P&F is likely to fluctuate from year to year, because the COLA is linked to the COLA for Social Security benefits. To demonstrate this likely fluctuation, the chart below compares the PERA General Plan COLA to the Social Security COLA since 2019.

Year	PERA General COLA	Social Security (CPI-W) COLA
2019	1.4%	2.8%
2020	1%	1.6%
2021	1%	1.3%
2022	1.5%	5.9%
2023	1.5%	8.7%
2024	1.5%	3.2%