Alternative Mechanism to Provide Future Cost-of-Living Adjustments (COLAs)

Senate Bill 18 *by Sen. Price & Sen. Cortez*

A proposal for Louisiana's state public retirement systems in the 2023 Legislative Session

In 2020, the Legislature tasked LASERS and the other three state retirement systems with developing a mechanism to provide meaningful COLAs to our retirees on a more regularly scheduled basis. Working together to achieve this goal, we have identified a model that maintains the legislative reforms and establishes a direct funding method for COLAs.

EXPLANATION

Current Model:

The current method for funding COLAs is complex and has not resulted in dependable, meaningful COLAs. Currently, the employer indirectly funds COLAs through a gainsharing arrangement where a portion of the System's excess investment earnings are used to pay for COLAs, rather than reduce the employer contribution rate. Excess investment earnings are those earnings over the expected rate of return.

One-half of the excess earnings above a statutorily determined dollar amount (hurdle) are deposited into the Experience Account – an account that holds funds to pay COLAs.

This model relies heavily on market conditions. As such, there is no guarantee if or when any deposits will be made into the Experience Account.

Proposed Model:

Under the proposal, the gainsharing funding model would end, and employers would fund COLAs directly rather than indirectly.

Funding would become a component of the annual employer contribution rate and be deposited directly into a newly created COLA account.

In 2029, the Initial Unfunded Accrued Liability (IUAL), will be paid off. As that date nears, employer contributions are projected to fall. The proposed legislation captures a portion of these, and other expected decreases to fund COLAs. [Additional employer contribution rate declines projected with 2040 payoff of another debt schedule].

Beginning in 2024, deposits into the COLA account would equal one-half of the decrease in the total employer contribution rate, growing until deposits reach a maximum of 2.5% of payroll.

FREQUENTLY ASKED QUESTIONS (FAQs)

Why is the proposed change necessary?

Put quite simply, the current method of funding COLAs is not working. It involves a complex granting matrix and relies too heavily on market conditions, which has resulted in LASERS retirees not having received a COLA in seven years.

Why now?

Passing the legislation in the current session is important since, due to legislative reforms, the employer contribution rate is expected to steadily decline following the 2024 reamortization of certain system gains. These steady declines will be followed by significant declines once debt is paid off in 2029 and 2040.

Will COLAs be automatic? Will COLAs become a guaranteed benefit?

No. COLAs will not be automatic. They would only be granted if there is enough funding in the account **AND** upon legislative approval.

No. COLAs will not become a guaranteed benefit. COLA funding will not constitute an actuarially required contribution.

Will eligibility criteria for a COLA change?

Yes. When the first COLA is paid from the new COLA account, eligibility criteria will change.

Regular retirees would need to be at least age 62 and retired at least two years.

Disability retirees would need to be retired at least two years, regardless of age.

COLA eligibility also extends to beneficiaries of retirees who would have met the above criteria, if alive; and survivors of non-retired members who have received a benefit for at least two years and whose benefit was derived from the service of a deceased member who would have been at least age 62.

How much will COLAs be?

COLAS will be up to 2% of the first $60,000 of the retirement benefit.

How often will COLAs be granted?

The proposed model is expected to generate enough funds to grant a COLA every two to three years, subject to legislative approval.

Can a COLA over 2% be granted?

Under the proposal, when sufficient funding is available, the LASERS Board of Trustees can recommend a COLA of up to, but no more than, 2%. However, the legislature may choose to authorize a COLA in excess of 2%, subject to gubernatorial approval.

What happens to the current Experience Account?

The Experience Account will be phased out. Any funds remaining in the Experience Account will be transferred to the new COLA account.

Will the proposed model add new debt to the system?

No. As with the current gain-sharing model, COLA funding is distinct from funding regular, monthly benefits. Funds for the actuarial cost of COLAS must be available before the legislature can grant a COLA, and that will not change. The allocation of funds to the COLA account via direct employer contributions does not create debt - unlike the current gainsharing model which generates interest. Moving away from the indirect funding model will allow more investment gains to be used to reduce existing debt.

Will the proposed model increase the cost of COLAs?

No. The cost of COLAs under the proposal will likely be less than the cost of the current model.

Will money be deposited into the new COLA account every year, and will there be a limit on how much can be deposited?

Deposits into the COLA account would occur every year, unless one of the employer safeguards prevents it. Safeguards include reducing or foregoing a deposit if it would cause the total employer contribution rate to exceed the established cap; also, the COLA account balance will be limited to the cost of paying two COLAs.

What can money in the COLA account be used to pay?

Funds in the newly created COLA account would be used to pay COLAs and to offset system investment losses, only in the event the system experiences a negative actuarial return.

Will the new COLA model undo past reforms?

No. Pension reforms enacted in 2009 and 2014 directed more excess investment earnings of the systems to pay down the UAL. These reforms will remain in place. The oldest debt schedules are on track to be paid on time.

Does the proposal include cost safeguards for employers?

Yes, the model includes built-in safeguards to protect employers.

The COLA rate cannot exceed 2.5% of payroll.

Prior to FYE 2039, the COLA rate shall not cause the total employer contribution rate to exceed the rate determined for FYE 2024. Beginning with FYE 2039, the COLA rate shall not cause the total employer contribution rate to exceed 22% of payroll.

When would the first COLA be paid under the proposed legislation?

There is no set time for payment of the first COLA under the proposed plan. A COLA can only be granted when there are sufficient funds to pay a COLA and when the legislature approves the granting of the COLA.