PUBLIC EMPLOYEES
RETIREMENT ASSOCIATION

Date: March 2, 2023
To: PERA Board of Trustees
From: Doug Anderson, Executive Director
Amy Strenge, Policy Coordinator
Subject: 2023 PERA Police & Fire Disability Modifications

Background

PERA Police and Fire disability benefits and the application process have received attention in recent years from stakeholders, PERA staff, and the Board of Trustees. As PERA staff reviewed the disability benefit provisions, they noted inadequacies in the process, inequities in some benefits, and insufficient offsets for some members. PERA staff have worked with stakeholders to explain the results of this review. With stakeholder engagement, PERA staff developed policy initiatives intended to provide a fair and transparent process and equitable benefits. The following initiatives have been reviewed with stakeholders and are generally supported. The proposed initiatives work together with the goal that the disability benefits provided by the Plan are both equitable and adequate for all members. PERA considered the purpose of disability benefits for members with and without reemployment earnings, the equity between active members and disability benefit recipients, and the impact to the Plan.

These proposed policy initiatives will be connected to HF 1234/SF 1959.

Vesting

Minn. Stat. §353.01, subd. 47 (d)(3), establishes a twenty-year graded vesting schedule for members of the Plan hired after June 30, 2014. After ten years, the member is fifty percent vested, and fully vested at twenty years.

Modifications to the vesting schedule have occurred several times throughout the Plan's history. Members hired before June 30, 2010, have a three-year vesting schedule. Members hired between July 1, 2010 and June 30, 2014 have a ten-year graded vesting schedule (members are fifty percent vested at five years, and fully vested at ten years).

Staff Recommendation for Vesting

The current twenty-year vesting schedule may not be the appropriate vesting schedule for the Plan because it is too long. The PERA staff recommends that the PERA Board lower the vesting schedule to a ten-year graded vesting schedule, which is more appropriate for the Plan. This change would allow a Police & Fire member to be fifty percent vested at five years and fully vested at ten years. Members currently not eligible for a retirement benefit would now be eligible for a retirement benefit. The estimated cost is 0.3% of payroll ($3M/year).

Duty Disability Benefit Eligibility

A member of the Plan is eligible to apply for a duty disability benefit if they have either:

- Not met the requirements for a retirement annuity under section Minn. Stat. § 353.651, subd. 1; or
- have "met the requirements under that subdivision, but does not have at least twenty years of allowable services credit." Minn. Stat. §356.656, subd. 1(b)(1).

An eligible Plan member who qualifies for a duty disability benefit receives a benefit that is sixty percent of the average salary, plus an additional three percent for each year of service in excess of twenty years. The sixty percent benefit, which is equivalent to a twenty-year benefit, is reported by PERA to the Internal Revenue Service ("IRS") as non-taxable income. Minn. Stat. §353.656, subd. 5a(b)(1-2) transitions the disability benefit to a retirement benefit at normal retirement age for members under normal retirement age or after 60 months for members over normal retirement age with less than twenty years of service. Currently, the retirement benefit is taxable. A member who receives a duty disability also receives continued health insurance from their former employer until age sixty-five per Minn. Stat. §299A.465.

The Secure Act 2.0 modified the treatment of service-connected disability benefits after the benefit has transitioned to a retirement benefit. Under prior law, the benefit became taxable when a disabilitant went from duty disability to retirement at normal retirement age. Effective for taxable years after 2026, the service-connected duty disability benefit retains its tax-exemption status even if the benefit converts to a retirement benefit under the plan.

This modification magnifies the inequity between members over fifty with more than twenty years of service (who are ineligible to apply for disability benefits) and members over fifty-five with less than twenty years of service (who may apply and receive disability benefits for 60 months).

While PERA's current legislative initiatives addressed the inequity by providing a member over fifty-five with less than twenty years of service the equivalent of a disability benefit as a retirement benefit instead of a 60-month disability benefit, this policy no longer resolves the disparate treatment.

Staff Recommendation for Duty Disability Eligibility

PERA staff recommends the PERA Board expand the eligibility for duty and regular disability benefits by permitting members to apply regardless of age and granting members a disability benefit for 60 months or until normal retirement age, whichever is later. The disability benefit would then convert to a retirement benefit. Modifying the eligibility for PERA P&F disability benefits would resolve the disparate treatment between members over fifty-five with more than twenty years of service and members over fifty-five with less than twenty years of service because all members would be eligible to receive a disability benefit at any age. This change is consistent with PERA's Correctional Plan, which allows members to be eligible for disability benefit regardless of age and service (members receive a disability benefit until normal retirement age or 60 months, whichever is later).

Duty Disability Benefit

Minn. Stat. §353.656, subd. 1, grants a duty disability amount of sixty percent of salary (a twenty year benefit) and an additional three percent for each additional year of service. A duty disability benefit for a member with more than twenty years of service reflects the additional years of service. The non-service connected portion (the minimum benefit) is non-taxable. For example, a member who has twenty-five years of service will receive seventy-five percent of their average salary, sixty percent of that benefit is non-taxable. Minn. Stat. §353.656, subd. 3, provides a maximum of forty-five percent for a regular disability benefit. Members do not receive credit for additional years of service.

Staff Recommendation for Duty Disability Benefit

PERA staff recommends capping the duty disability benefit similar to the way the regular disability benefit is capped. The duty disability benefit would be a maximum of sixty percent and additional years of service would not be reflected in the benefit. Once a member transitioned to a retirement benefit, the member's retirement benefit would reflect all years of service.

Duty Total and Permanent Disability Benefit

Minn. Stat. §353.656, subd. 1a establishes that a duty total and permanent disability benefit is sixty percent of the average salary, which is the same as a duty disability benefit. However, unlike a duty disability recipient, a duty total and permanent disability benefit recipient does not have reemployment earnings. .

Staff Recommendation for Duty Total and Permanent Disability Benefit

Recent discussions on the adequacy of disability benefits for public safety members has identified an inadequacy for certain members receiving total and permanent duty disability benefits. It is an important distinction whether a member has reemployment earnings or is unable to have reemployment earnings when considering the whether the disability benefit is sufficient. Reemployment earnings offer the opportunity for a member to supplement their disability benefit with employment. Reemployment earning are not available, however, to members receiving duty total and permanent disability benefit since they are not able to engage in any substantial gainful employment. A comparison of disabilitants with earnings from reemployment and those without similar earnings shows that for duty total and permanent disabilitants, the current disability benefit of sixty percent is inadequate. Minn. Stat. §353.651, subd. 3(b), caps a Plan member's retirement benefit at ninety-nine percent of the member's average salary. PERA staff recommends an increase in the duty total and permanent benefit to ninety-nine percent of the member's salary.

Disability Offsets

Minn. Stat. §353.656, subd. 2 and 4, provide limitations on the amount of the Plan disability benefit payment. If a member does not have reemployment earnings or a workers' compensation benefit there is no pension benefit offset. Members receiving the disability benefit with a workers' compensation benefit are able to receive up to one hundred percent of the base salary currently paid by the employing governmental subdivision for a similar position before an offset is applied.   If the member receives more than the threshold, the member's benefit is offset one dollar for every dollars over the threshold.

If there are reemployment earnings with or without workers' compensation benefits, members are able to receive up to one hundred and twenty-five percent of the member's salary or the base salary currently paid by the employing governmental subdivision, which is higher. If the member exceeds the threshold, the benefit is offset one dollar for every three dollars. Very few members have earnings over the current threshold.

The current threshold has proved problematic for several reasons. By offsetting for workers compensation, the benefits are offset because of an injury-related benefit. The member does not determine the workers compensation benefit. PERA's focus should instead be on the member's ability to earn from employment. If a member is able to earn from reemployment, the disability benefit should reflect the reemployment earnings.

The current offset approach fails to reflect two important equity comparisons with active members. First, the basic concept of a retirement plan is that active members contribute to the Plan while working to help support benefits when unable to work due to disability or retirement. Currently, disability recipients make no such contribution even if working. A disability recipient is now in a position to retain all of their earnings without helping to fund future benefits while current active members must contribute not only for their benefit, but for the disability recipient's benefit. A disability recipient that is working cannot be asked to contribute directly to the Plan. However, their benefit can be offset to be more on a par with how active members participate in the funding of the Plan.

Second, a disabilitant currently has the opportunity to use the disability recipients benefit as a base toward earning more than an active member in a comparable position. Currently, a disabilitant can out-earn an active member even if they have as little as 25 percent of their prior earnings as reemployment earnings.

See the attached exhibit for an example of the current and proposed offsets.

Staff Recommendation for Disability Offsets

PERA staff recommends a change to replace the current approach with two offsets. The offsets only apply if a member has reemployment earnings. Workers' compensation benefits would no longer be a component of an offset. The first offset to the disability benefit is equal to reemployment earnings up to 11.8 percent of the average salary used to determine the member's disability benefit . The applicable rate would change if the member's contribution rate changes.

The second offset amount is a reduction of one dollar for each dollar that the disability benefit plus reemployment earnings (without regard to offset number one above) exceeds one hundred percent of pay for an active member in a comparable position.

Disability Reapplication

Minn. Stat. §353.031, subd. 8, requires the disability benefit recipients to provide proof that they remain disabled. The statute requires members submit one written report by a licensed physician, an APRN, or a licensed chiropractor, or, with respect to a mental impairment, a licensed psychologist when required by PERA. The statute is mute on how often this process should occur. Current administrative process requires a member to provide proof once a year for the first five years, and every three years after that.

The process outlined in statute essentially requires that members reapply for the disability benefit and again prove that they are disabled. However, the perception and experience has been that members may assume they are entitled to continue to receive disability benefit. This perception has been highlighted in PERA's experience with the Office of Administrative Hearings where the administrative law judges have determined that PERA bears the burden of proving that the member is no longer disabled.

Staff Recommendation for Disability Reapplication

The PERA staff recommends modifying Minn. Stat. §353.031, subd. 8 to set clear expectations for all of PERA's members and clarify requirements. The recommended changes will clearly state that the member is responsible to reapply for the disability benefit once a year for the first five years and once every three years after that. Language will clarify that the burden of proof remains with the member in the event of an appeal.

PERA Duty Disability Retirement Benefit
Example of Current and Proposed Disability Benefit Offsets
Prepared by PERA Staff, February 17, 2023

Member Inputs:	
Position Salary	$ 100,000
High 5	$ 93,462
Disability %	60%
Disability Benefit	$ 56,077

Current Offset:
One-third of amount that Disability Benefit plus Re-employment Earnings exceeds Position Salary

Proposed Offsets:
Offset #1 = Minimum of (A) 11.8% of Position Salary or (B) Re-employment Earnings
Offset #2 = 100% of the amount that Disability Benefit plus Re-employment Earnings exceed 100% of Position Salary

	Active Member	**Duty Disability Retiree - Current Offset**					**Duty Disability Retiree - Proposed Offsets**				
	A1	**B1**	**B2**	**B3**	**B4**	**B5**	**C1**	**C2**	**C3**	**C4**	**C5**
Member Salary	$ 100,000	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
PERA Contribution	(11,800)	-	-	-	-	-	-	-	-	-	-
Taxable Earnings	$ 88,200	-	-	-	-	-	-	-	-	-	-
Re-employment Earnings	N/A	$ 0	$ 30,000	$ 60,000	$ 90,000	$ 120,000	$ 0	$ 30,000	$ 60,000	$ 90,000	$ 120,000
Disability Benefit	N/A	$ 56,077	$ 56,077	$ 56,077	$ 56,077	$ 56,077	$ 56,077	$ 56,077	$ 56,077	$ 56,077	$ 56,077
Current Offset	N/A	0	0	0	(7,026)	(17,026)	[redacted]				
Proposed Offset #1	N/A	[redacted]					(0)	(11,028)	(11,028)	(11,028)	(11,028)
Proposed Offset #2	N/A						(0)	(0)	(16,077)	(45,048)	(45,048)
Net Disability Benefit	N/A	$ 56,077	$ 56,077	$ 56,077	$ 49,051	$ 39,051	$ 56,077	$ 45,048	$ 28,972	$ (0)	$ (0)
Taxable Earnings	$ 88,200	$ 0	$ 30,000	$ 60,000	$ 90,000	$ 120,000	$ 0	$ 30,000	$ 60,000	$ 90,000	$ 120,000
Non-taxable Earnings	-	56,077	56,077	56,077	49,051	39,051	56,077	45,048	28,972	(0)	(0)
Total Earnings	$ 88,200	$ 56,077	$ 86,077	$ 116,077	$ 139,051	$ 159,051	$ 56,077	$ 75,048	$ 88,972	$ 90,000	$ 120,000

Key Points:

1. A disability retiree's financial advantage begins at a relatively low Re-employment Earnings level - about 25% of current pay. **(B2 > A1, after considering taxes)**
2. Members with no re-employment earnings are not impacted by the proposed change **(B1 = C1)**
3. When a disability retiree's reemployment earnings exceeds that of a member's pay, the disability benefit is zero. **(C4 & C5)**
4. Disability retirees still maintain a tax advantage. **(C3 > A1)**
5. Proposal may not adequately incentivize a member to increase re-employment earnings once Offset #2 applies **(C4 < C3, after considering taxes)**