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COLA Changes – What You Need to Know

How is the Cost-of-Living Adjustment (COLA) Changing?

At the Sept. 15, 2016 Board meeting, SERS' Board of Trustees approved seeking the following legislative changes to SERS' COLA:

1. COLA – Indexed to the Consumer Price Index (CPI-W) not greater than 2.5% with a floor of 0%.
2. Retirement allowances or benefits that begin on or after Jan. 1, 2018 shall receive a COLA, with the first COLA applied on the fourth anniversary date following start of the retirement allowance or benefit. In no case shall a person miss more than three cost-of-living adjustments in total.
3. No COLA shall be applied to a retirement allowance or benefit that began before Jan. 1, 2018, for three consecutive years, with such suspension beginning Jan. 1, 2018, and payment of COLAs resuming on anniversary dates on and after Jan. 1, 2021.

Why are These COLA Changes Necessary?

While SERS is not in financial crisis, the COLA changes are necessary to address immediate financial challenges and long-term funding goals.

Immediate Financial Challenges

One immediate challenge SERS faces is that the System is susceptible to moving outside of the state's mandated 30-year funding window. Moving outside of the mandated 30-year window would require SERS to present a financial plan to the Ohio Retirement Study Council (ORSC) to get the System back within the 30-year window. SERS' plan would be reviewed by ORSC actuaries to verify that it would work, and possibly subject the System to additional pension changes.

Another immediate challenge is that, at its present funding level, SERS has little cushion to weather another major financial recession. Following the Great Recession, SERS' funding decreased from 82% in 2008 to 63% in 2012. As of June 30, 2015, SERS was 68% funded over 27 years. That funding level will go down based upon the following funding pressures:

1. During the last two years, minimal investment returns of 3.87% in FY2015 and 1.38% in FY2016 stalled SERS' funding progress.
2. The actuary recommended, and the Board approved, a reduction to SERS' assumed rate of return from 7.75% to 7.5%, which further decreased the System's funded status.

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3. Investment consultants have warned that investment returns in the next 3-5 years could be below the 7.5% assumed rate of return, which will put further strain on the System’s funded status.

Finally, at the current funding level, SERS is unable to provide any employer contributions to support health care. While the Health Care Fund has other funding sources, funding from employer contributions is historically one of the largest sources of income for health care.

Long-Term Funding Goals

Ultimately, SERS’ funding policy states that the long-term goal is to get to 90% funded. To speed up the funding progress, the Board changed the funding policy so that all 14% of employer contributions would be used to fund pensions with nothing going to health care until the pension fund reaches 70% funded. An increased amount of employer contributions can be devoted to health care when funding achieves the 80% and 90% levels.

What Will the COLA Changes Do?

On the present course with no changes, SERS’ actuary predicted the System would not reach 70% funded until 2030. This would likely cause major changes to SERS’ health care. With the COLA changes, the System is expected to reach 70% funded by 2018 and 90% funded by 2034. The 90% level is critical because, at that level, the pension fund is stable and can withstand a market downturn.

Why Were Retirees Who Live on a Fixed Income Included in the COLA Changes?

There are several reasons the COLA changes include retirees:

1. In 2012, the age and service eligibility pension reform changes affected only active members.
2. SERS’ actuary determined that more than 60% of the System’s unfunded liabilities are the responsibility of retirees, and any additional pension reform changes needed to include retirees.
3. The COLA changes address the financial challenges SERS faces, and equally and fairly affect active members and retirees.

How Many Times Has the COLA Changed?

Since the COLA was introduced in 1971, there have been a total of eight COLA and ad hoc changes. Changes included implementing and removing waiting periods (from one year to three years), raising and lowering fixed rates (from 1.5% to 3%), using a rate tied to the CPI-W, and one-time increases to allow older retirees to “catch up” with new retirees.

When Will These Changes Take Effect?

Changes to the COLA require legislative approval. It is unknown at this time how long that approval will take. Our estimate is that the COLA changes will take effect Jan. 1, 2018.

SERS’ COLA and Ad Hoc History

April 1, 1971

- First COLAs granted

1976

- Increased from 1.5% to 2.0%
- Waiting period reduced from 3 years to 2 years

1979

- Increased from 2.0% to 3.0%
- Waiting period decreased from 2 years to 1 year

1981

- 6% ad hoc increase for those retired on or before January 1, 1977
- 4% ad hoc increase for those retired after January 1, 1977

1984

- 5% ad hoc increase for those retired on or before January 1, 1983

1988

- 2% ad hoc increase for those retired on or before February 1, 1983
- 5% ad hoc increase for those retired after February 1, 1983

1996

- COLA tied to CPI-W
- Instituted COLA bank if CPI-W COLA was below 3%

2002

- Fixed COLA at 3%
- Eliminated COLA bank

2006

- Allowed alternate payees receiving a benefit as part of a division of property order to receive COLAs