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MEMO

TO: House Ways and Means Committee

FROM: Christian Larson, Director

DATE: February 17, 2025

SUBJECT: Fiscal Notes for Paid Leave Modifications

During the 2024 legislative session, bills were introduced making modifications to the Paid Leave program administered by the Department of Employment and Economic Development (DEED). Fiscal notes were requested and completed on these bills. Legislative members raised concerns regarding the contents of the fiscal notes. Specifically, concerns were raised about underlying assumptions on the fiscal notes for HF5363-4A, SF5430-7A, and SF5430-16A.

This memorandum provides relevant background information regarding the fiscal note development, identification of challenges in the fiscal notes, and provides possible actions that the LBO, LBO Oversight Commission (LBOOC), the legislature, and agencies can take to limit similar issues in the future.

In summary, fiscal notes for proposed changes to this program are complex because of an unclear baseline, substantial changes in assumptions that occurred between the 2023 end of session estimates and the 2024 fiscal notes, and an assumption about the use of permissive authority allowed in the enacting legislation. These changes are described further on the subsequent pages.

Background

Prior to the 2024 session, DEED prepared fiscal notes for the proposed paid family and medical leave programs internally, using various modeling techniques. This type of analysis is what the LBO and the legislature, in general, were accustomed to seeing from the agency for establishment of the paid leave program prior to 2024.

In fiscal notes developed from 2019 through 2022, DEED used a simulation model developed by the Institute for Women's Policy Research in partnership with the US Department of Labor (USDOL) to estimate program usage. In 2023, DEED transitioned to modeling the proposed paid leave program internally using the USDOL WorkerPLUS Model, a similar model to that used previously in fiscal note estimates.

In the 2023 enacting legislation, an actuarial analysis was required to determine whether the program, as established, was actuarially sound. That analysis was completed by Milliman, Inc and released in October 2023. The October actuarial analysis provided an estimate of the program under two scenarios. First, it estimated premium collection as established in Laws of Minnesota 2023, chapter 59, art. 1, sec. 23, subd. 6 and subd. 7. Second, it estimated premium collection under an alternative scenario with a different initial premium rate and an alternative premium rate setting structure than was included in the law. The actuarial analysis suggested the alternative premium rate structure was preferable as it targeted a higher fund balance in the first year of the program, when program activity is less certain and because the alternative proposed premium rate resulted in less fluctuation of the premium rate in the first four years of the program, which is preferable for employers and employees.

Early in the 2024 session, the LBO met with DEED to discuss how they would approach developing estimates for proposed changes to the Paid Leave program established in Laws of Minnesota 2023, chapter 59. At that time, DEED expressed concern with internally running the same type of analysis that was done previously using the USDOL WorkersPLUS Model, given that an actuarial study had been published. They also expressed concern about the resources required to pay for additional third-party actuarial analyses to be created in response to future fiscal note requests.

Three issues regarding aspects of the program and the program implementation were identified in that meeting, or later during the development of the fiscal notes, that would make the development of the fiscal notes challenging:

1. There was not an apparent and obvious baseline number for the fiscal impacts of the Paid Leave Law. The program is an entitlement program that does not have a historical record in Minnesota to use as the baseline as it has not yet been implemented, and the fiscal estimates for the program were not included in the Minnesota Management and Budget (MMB) budget and economic forecast until November of 2024.
2. During the implementation process, prior to the 2024 session, DEED refined its understanding regarding certain program provisions. The Paid Leave Law requires a seven-day qualifying event. Fiscal note estimates developed for the 2023 legislative session assumed that there were no unpaid days for eligible recipients. Following the 2023 passage of the bill, in reviewing the statutory language and working with actuarial consultants, DEED clarified the seven-day qualifying event to mean that those first seven days were unpaid days for which the recipient would receive no benefit payment.
3. The 2024 fiscal notes assumed that DEED would use permissive authority included in the enacting legislation to adjust the first-year premium rate of the Paid Leave Law and adjust future year premium rates if the program was found not to be actuarially sound.

Challenges with 2024 Paid Leave Law Fiscal Notes

1. **Establishing Baseline Costs and Revenues for the Paid Leave Law**

   Fiscal notes must estimate the fiscal impact of proposed legislation to the state as measured from current law. To do so, a clear baseline must first be established. It was apparent that the establishment of a baseline for costs and revenues for the Paid Leave Law would be difficult, both because the program is an entitlement program that has not yet started, and because there were multiple options to use as a baseline.

   Funds were appropriated for the Paid Leave Law based on estimates in the fiscal notes from the 2023 session, which used the USDOL WorkerPLUS model. Subsequently, and as required by the 2023 enacting legislation, an actuarial study was released in October 2023 by Milliman, Inc to determine costs of providing benefits and maintaining solvency of the fund. This included estimates of premium collections and benefit payments and an analysis of whether the program as established was actuarially sound.

   The question became whether the 2024 fiscal notes should measure a change from the 2023 end of session fiscal estimates or from the actuarial analysis that was released in October 2023.

   The LBO consulted with DEED, non-partisan fiscal staff in the House and Senate, and the MMB Budget Division to help determine what the baseline should be for the Paid Leave Law fiscal notes during the 2024 session. All parties agreed that the best baseline would be the cost estimates generated in the alternative scenario published in the October 2023 actuarial analysis, which was perceived to be the most recent and likely most accurate information available.

   The parties recognized this could be confusing for members but thought it was important to treat the Paid Leave Law similar to other entitlement programs. The October actuarial analysis was the best and most recent data available for the Paid Leave Law; therefore, it was the most appropriate baseline for fiscal notes developed in the 2024 session. This is consistent with fiscal note practice for forecasted programs, in that fiscal notes for forecasted programs rely on the most recent MMB budget and economic forecast, as opposed to end of session fiscal estimates, for fiscal note development.

   It should be noted that MMB budget and economic forecasts do not include all non-general fund fund statements. MMB makes a determination of what is included based upon the fund type and relevance to operating budget decision-making.

   In addition to the above, the LBO later learned that Milliman, Inc was creating estimates for the costs for the proposed adjustments in the 2024 bills HF5363 and SF5430. From a consistency standpoint, the use of the October 2023 actuarial analysis alternative scenario seemed like the most logical baseline from which to measure changes.

2. **Refinement of Paid Leave Law Assumptions Following Passage of HF2 in 2023 Legislative Session**

   In the development of the fiscal notes in 2023, DEED interpreted the Paid Leave Law to allow for eligible workers to receive benefits beginning the first day of their qualifying event. Laws of Minnesota 2023, chapter 59, art. 1, sec. 14, subd. 2 requires that a qualifying event last at least seven days for eligible leaves other than those related to bonding. The 2023 fiscal notes assumed, but did not make explicit, that eligible workers could retroactively receive payment for those seven days.

   Upon passage, DEED worked toward implementing of the language and their assumptions and interpretations of the bill were refined. Through review of the statutory language and working with the actuarial consultants, the agency determined that the enacting legislation included a seven-day waiting period for which the recipient would receive no benefit payment for a qualifying event. Therefore, the October 2023 actuarial analysis for the Paid Leave Law assumed that the seven-day qualifying event requirement established a seven-day, unpaid, waiting period for eligibility for all non-bonding leaves.

   This became a challenge for the 2024 fiscal notes because part of the 2024 language clarified that there was no waiting period (or for SF5430-7A no waiting period for certain beneficiaries). The increased cost of having no waiting period is technically a new cost under this updated assumption. However, it is not a new cost as originally understood by the legislature when it passed the law in 2023. The LBO worked with DEED to make sure that the 2024 fiscal notes were explicit in the change in this assumption between the 2023 and 2024 fiscal notes.

   It should be noted this refinement of assumptions is not a completely uncommon occurrence. As agencies have additional time to review and understand the requirements of laws following a law's passage, there are times that assumptions are refined or adjusted which can have significant fiscal effects. The fiscal impacts resulting from refinements of bill interpretation often get included and reported in the budget and economic forecast for forecasted general fund programs and any non-general fund forecasted programs included in the budget and economic forecast.

3. **DEED Authority to Adjust First Year Premiums**

   The original Paid Leave Law (Laws of Minnesota 2023, chapter 59, art. 1, sec. 23, subd. 6) established a premium for the first year of 0.7 percent of all taxable wages for an employer participating in both the family and the medical leave benefit program. Premium collection is set to begin on January 1, 2026. In the enacting legislation, after the first year of the program, the commissioner of DEED must adjust the premium using a formula established in law (Laws of Minnesota 2023, chapter 59, art. 1, sec. 23, subd. 7) and the premium rate cannot exceed 1.2 percent of taxable wages paid to each employee. The fiscal notes from the 2023 session assumed an initial premium rate of 0.7 percent and carried the 0.7 percent for each year of the fiscal note tables.

The October 2023 actuarial analysis developed an estimate of the premiums collected for the Paid Leave Law assuming a first-year employer premium rate of 0.7 percent of taxable wages followed by a change in the rate based on the formula in statute in subsequent years. Premium rates were estimated to fluctuate between 0.7 percent and 0.92 percent for the first four years of the program, and then flatten out to 0.84 percent starting in year five based on the actuarial estimates of program usage.

The October 2023 actuarial analysis also included an alternative premium structure that targeted a higher fund balance in the first year of the program and would limit premium volatility in the first five years of the program. The alternative proposed premium rate structure estimated an employer premium rate of 0.78 percent for the first three years of the program and a rate of 0.83 percent thereafter.

The fiscal notes included the use of the alternative method for premium rates. In the fiscal notes, DEED explained they have permissive authority to adjust the first-year premium rate based on the findings of the October 2023 actuarial analysis. In the fiscal notes, DEED cited Laws of Minnesota 2023, chapter 59, art. 1, sec. 41, paragraph (c), which states:

> *If the actuarial study indicates that the premium rate of Minnesota Statute, section 268B.14, subdivision 7, is not actuarially sound, the commissioner, in consultation with the commissioner of management and budget, must adjust the premium rate to make the program actuarially sound, subject to limitations in Minnesota Statutes, section 268B.14, subdivision 7, paragraph (b).*

The agency concluded based on the results of the October 2023 actuarial analysis that the program as enacted was not actuarially sound. This, therefore, did not meet the criteria for actuarial soundness and would suggest the agency's ability to move forward with using the permissive language in the bill.

Under DEED's interpretation, using the alternative premium calculation meant the adjustment from 0.7 percent to 0.78 percent would *not* be measured by fiscal notes in the 2024 session as the change was not a result of the 2024 bill language.

The LBO expressed concern with this assumption given there had been no public discussion or announcement from the agency prior to the release of the 2024 fiscal notes that they had the authority, and would exercise the authority, to adjust the first-year premium rate. Even with the authority to do this, a fiscal note is not the appropriate avenue to announce that first-year premiums would be different than previously discussed in any public setting.

Without a prior statement about an adjustment to the first-year premium rate from the agency, it was an unintended outcome that the fiscal note became the first public statement that such an adjustment was being made.

It should be noted that subdivision 7 of Minnesota Statutes 2023, section 268B.14 references premium adjustments after the first year of the program. Minnesota

Statutes 2023, section 268B.14, subdivision 6 is the reference to first year premiums. DEED assumed that the intent of the 2023 bill was to allow for the first-year premium to be adjusted if it was found not to be actuarially sound in the actuarial analysis that was statutorily required in the fall of 2023.

In the end, the use of the October 2023 alternative scenario was included in the 2024 Paid Leave Law fiscal notes given it was the most likely scenario for the agency to implement the bill as enacted.

Possible Actions to Address Issues

Many of the issues with the Paid Leave Law fiscal notes originated from the program being a complex piece of legislation and because it is an entitlement program without historical activity in Minnesota. Traditionally, for an entitlement program, a baseline fiscal estimate would be the actual historical activity, and any projected changes.

Fiscal estimates for the Paid Leave Law were not included in MMB's budget and economic forecast until the November 2024 Forecast when MMB published the Family and Medical Benefit Insurance Fund Statement. Adding to the complexity is that there were two different previous estimates of the Paid Leave Law – the 2023 end of session enacted budget and the October 2023 Milliman actuarial analysis. Together, these created a relatively unique set of infrequent circumstances.

The pieces of this scenario that *could* reoccur are twofold. The first is an agency refining its interpretation of a bill after passage of the bill but before the program goes live, as was the case with the seven-day waiting period. The second is an agency assuming for purposes of a fiscal note it would exercise permissive authority, as was the case with the adjustment of the first-year premium rate.

The following are items identified to address these issues with the fiscal note process moving forward:

1. The LBO should be more assertive in their communication to agencies to set clear expectations of what information is required for a fiscal note to meet fiscal note standards and would provide the necessary level of detail in the fiscal note.

2. The LBO could provide a more detailed and developed analysis alongside a fiscal note in certain situations:

    a. In circumstances, such as the case with the 2024 Paid Leave Law fiscal notes, where the fiscal note is deemed by the LBO to meet fiscal note standards, but additional analysis is useful, the LBO could develop additional research and analysis for committees to provide useful analysis and detail not captured in the fiscal note.

    b. In circumstances where the fiscal note is deemed to not meet fiscal note standards and an agreement between the agency and LBO cannot be made to get the note to a point the LBO will approve the fiscal note, the

LBO can release the fiscal note “unapproved” along with a cover memo describing the concerns that remain with the fiscal note estimates and provide additional information or estimates when the necessary information is available to the LBO to make such estimates.

3. For significant fiscal notes or fiscal notes for new programs, agencies should engage with the LBO early in the process to provide their preliminary assumptions and general approach to developing the fiscal note estimates.

4. Agencies should communicate with legislative members and staff regarding substantial changes to assumptions related to existing programs prior to the release of the fiscal note. The LBO should be included in these communications.

5. The Legislature and the LBOOC could reiterate their expectation that fiscal notes are to be made without political consideration. Fiscal notes are to be approached with the sole intent of providing a clear estimate of the fiscal effect of legislation and to provide a clear understanding of the assumptions and methodology used in the fiscal note estimate.

6. The LBO Oversight Commission could instruct a working group including a subset of state entities responding to fiscal note requests, non-partisan fiscal staff, MMB, and the LBO to develop additional standards for fiscal notes related to following situations:
    a. An agency has substantial updates to assumptions previously used in fiscal note estimates or in estimates included in the budget and economic forecast.
    b. A substantially complex or new program is proposed.
    c. Expectations for agencies regarding fiscal note development when estimates may require a third-party to develop fiscal estimates.

7. DEED should share their plan for estimating the fiscal impact of proposed changes to the Paid Leave Law during the 2025 session and beyond.