

DATE: February 24, 2021

TO: Senator Joseph Rafferty, Chair
Representative Mike Sylvester, Chair
Members, Joint Standing Committee on Labor and Housing

FROM: Kathy J. Morin, Manager, Actuarial and Legislative Affairs

SUBJECT: Testimony on L.D. 397 – An Act to Recalculate Retirement Benefits for Certain
State Employees Adversely Affected by Merit Pay Freezes

Senator Rafferty, Representative Sylvester, and members of the Joint Standing Committee on Labor and Housing. My name is Kathy Morin, and I am the Manager of Actuarial and Legislative Affairs for the Maine Public Employees Retirement System.

MainePERS is neither for nor against L.D. 397. We are here to provide information and offer any assistance the Committee might need regarding this bill.

Included with this testimony is a report that MainePERS submitted to the Joint Standing Committee on Appropriations and Financial Affairs in January 2017. That report was the result of Resolve, Chapter 78, which directed MainePERS to work with the Department of Administrative and Financial Services (DAFS) to identify retirees for whom retirement benefits were impacted by pay freezes, and to determine the costs associated with including those lost wages in benefit calculations. No legislative action was taken in response to the report, but we are providing it to you today as background information for L.D. 397.

By way of information, this issue was considered by the 129th Legislature in the form of L.D. 1339, which was voted out of Committee ought not to pass. While the 2017 report included approximately 1600 retirees, L.D. 1339 would have impacted approximately 530 of the retirees included in that report.

L.D. 397 would impact approximately 80 of the approximately 1600 retirees included in the original report. The bill would permit retirees who retired between May 1, 2014 and June 30, 2014 and whose benefits were impacted by certain pay freezes to include those lost wages in their benefit calculation.

L.D. 397 will have a fiscal impact because the Constitution does not allow the creation of new or additional benefits unless immediately and fully funded. Based on the retiree data used in the preparation of the 2017 report, we estimate an approximate \$600,000 increase to the UAL for retroactive application as provided in the bill.

The original analysis included lost pay for both merit and longevity pay freezes, while L.D. 397 includes only lost wages due to frozen merit pay. We do not expect excluding longevity pay will significantly reduce the costs estimated from the 2017 analysis.

Thank you for your consideration of this testimony. I would be happy to answer your questions and will be available at your work session.

January 31, 2017

Senator James Hamper, Senate Chair
Representative Drew Gattine, House Chair
Members, Joint Standing Committee of Appropriations and Financial Affairs
5 State House Station
Augusta, ME 04333-0005

Dear Senator Hamper, Representative Gattine, and Members of the Appropriations Committee:

Please accept the enclosed report on the inclusion of lost wages in retirement benefit calculations, which MainePERS developed and prepared in collaboration with the Department of Administrative and Financial Services, in response to Resolve, Chapter 78.

We would be pleased to respond to any questions you might have about the report.

Respectfully,



Kathy J. Morin
Manager, Actuarial and Legislative Affairs

Encl.

cc: Robert Weaver, Director of Governmental and Legislative Affairs

Overview

The Maine Public Employees Retirement System administers defined benefit plans for State employees, public school teachers, judges, legislators and employees of participating local districts. Defined benefit plans provide for a fixed benefit calculated based upon service credit, earnable compensation and a benefit accrual rate. For most MainePERS members, benefits accrue at a rate of 2% for each year of service credit. Increased years of service and earnings result in increased benefit levels.

Background – Lost Merit/Longevity Pay as Earnable Compensation

Earnable compensation, that is, earnings received for services rendered, is a key component in the calculation of retirement benefits. The highest three years of earnable compensation are used to calculate the average final compensation used in the calculation of retirement benefits. When earnable compensation is lower in some years than it might otherwise have been, the result can be a lower retirement benefit.

P.L. 2009, chapter 213, Part SSS amended the statutory definition of average final compensation to include wages lost by State employees for various reasons, including “...days off without pay or days worked for which the level of pay is reduced as a result of the freezing of merit pay and longevity pay as authorized by legislative action...” (5 MRS § 17001, sub-§4). Chapter 213 also instituted ten (10) State government closure days during fiscal years 2009-2010 and 2010-2011, and froze merit increases and longevity payments for the period July 1, 2009 through June 30, 2011. The amendment permitted lost wages in those fiscal years to be included as earnable compensation, and thus used in the calculation of the average final compensation for impacted retirees. In order for wages lost due to merit pay freezes and longevity pay freezes to be included in the retirement benefit calculation, the retiree is required to pay the employee portion of the contributions due on those lost wages.

P.L. 2011, chapter 380, Part E continued the freeze on merit pay and longevity payments for the period July 1, 2011 and June 30, 2013. While longevity payments were subsequently restored, the freeze on merit pay remained in effect. Chapter 380 did not include a provision that permitted lost wages during this period to be included as earnable compensation. Therefore, for those individuals retiring on and after July 1, 2011, average final compensation and retirement benefits were potentially lower as a result of the lost wages.

During the 127th Legislature, P.L. 2015, chapter 267, Part CCCC, section 1 and P.L. 2015, chapter 385 were enacted to permit individuals who retired on and after July 1, 2015 to include wages lost due to merit pay freezes and longevity pay freezes during fiscal years 2011-2012 and 2012-2013 in their retirement benefit calculations. As a result of the enactment of these laws, retirees on and after July 1, 2015 are permitted to include lost wages for all applicable years in

their retirement benefit calculation. However, individuals who retired after June 30, 2011 and prior to July 1, 2015, were not afforded this same opportunity.

Recent Legislative Action

To address the perceived “gap” for individuals who retired between July 1, 2011 and June 30, 2015, L.D. 1677 was proposed during the Second Regular Session of the 127th Legislature, and was enacted by the Legislature as Resolve, Chapter 78, effective April 15, 2016, as follows:

Resolve, Directing the Department of Administrative and Financial Services and the Maine Public Employees Retirement System To Identify Retirees Whose Retirement Benefit Calculations Were Adversely Affected by Certain Pay Freezes and To Calculate Costs Associated with Authorizing Those Retirees To Include Such Lost Wages in Retirement Benefit Calculations

Preamble. Whereas, the law governing the calculation of member retirement benefits was amended by Public Law 2015, chapter 267, Part CCCC, section 1 and chapter 385 to allow members of the Maine Public Employees Retirement System who retired on or after July 1, 2015 to pay the necessary member contributions to include in their retirement benefit calculations wages lost due to merit pay freezes and longevity pay freezes; and

Whereas, equity requires that the law be similarly amended to allow members of the Maine Public Employees Retirement System who retired prior to July 1, 2015 to pay the necessary member contributions to include in their retirement benefit calculations wages lost due to such pay freezes; and

Whereas, in order to rectify the situation, it is necessary first to determine the population of retirees who are potentially affected by this inequity, and then to calculate the costs associated with expanding the universe of retirees who are permitted to elect to contribute the necessary member contributions to include in their retirement benefit calculations wages lost due to such pay freezes; now, therefore, be it

Sec. 1 Identification of members. Resolved: That the Department of Administrative and Financial Services and the Maine Public Employees Retirement System shall work together to identify retirees who retired prior to July 1, 2015 and whose retirement benefit calculations were adversely affected by merit pay freezes and longevity pay freezes in effect in fiscal years 2011-12 and 2012-13; and be it further

Sec. 2 Calculation of costs. Resolved: That the Department of Administrative and Financial Services and the Maine Public Employees Retirement System shall work together to calculate the projected costs associated with authorizing members of the Maine Public Employees Retirement System who retired prior to July 1, 2015 to include in their retirement benefit calculations wages lost due to merit pay freezes and longevity pay freezes in effect in fiscal years 2011-12 and 2012-13; and be it further

Sec. 3 Report. Resolved: That, no later than January 12, 2017, the Department of Administrative and Financial Services and the Maine Public Employees Retirement System shall report their findings pursuant to sections 1 and 2 to the joint standing committee of the Legislature having jurisdiction over retirement matters. The joint standing committee of the Legislature having jurisdiction over retirement matters may report out to the First Regular Session of the 128th Legislature a bill to authorize members of the Maine Public Employees Retirement System who retired prior to July 1, 2015 to include in their retirement benefit calculations wages lost due to merit pay freezes and longevity pay freezes in effect in fiscal years 2011-12 and 2012-13.

Results of Analysis

MainePERS worked with the Department of Administrative and Financial Services to identify the retirees who retired prior to July 1, 2015 whose retirement benefit calculations were potentially adversely affected by merit pay freezes and longevity pay freezes in effect in fiscal years 2011-12 and 2012-13. Of the approximately 1900 individuals who retired during the applicable timeframe, approximately 1600 would potentially benefit from a change in law. Due to the amount of resources necessary to identify this population, some estimations and assumptions have been applied both in the identification and cost calculation process.

Costs are being provided based on two scenarios: (1) application to benefit payments retroactively to the date of retirement; and (2) application only to prospective benefit payments. If a change is implemented such that benefits to the impacted retirees are recalculated retroactive to effective dates of retirement, the change would result in an increase in the unfunded actuarial liability (UAL) in the amount of approximately \$13.1 million. If a change is implemented such that benefits are recalculated on a prospective basis, the change would result in an increase in the UAL in the amount of approximately \$9.7 million. The cost to retirees (i.e., employee contributions on the lost wages plus interest) would be approximately \$100,000.

Under Article 9, Section 18-A, of the Maine Constitution, the State would be required to pay the UAL cost in its entirety at the time the plan change became effective.

Implementing Legislation

If the Committee decides to move forward on this matter, MainePERS is prepared to assist in the preparing of legislation to authorize members who retired prior to July 1, 2015 to include in their retirement benefit calculations wages lost due to merit pay freezes and longevity pay freezes in effect in fiscal years 2011-12 and 2012-13.