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Final Report of the Task Force to Study Parity and Portability Of Retirement Benefits For State Law Enforcement Officers, Municipal and County Law Enforcement Officers And Firefighters

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Executive Summary

The Task Force to Study Parity and Portability of Retirement Benefits for State Law Enforcement Officers, Municipal and County Law Enforcement Officers and Firefighters was created by Resolve 2003, chapter 76 in the 1st Regular Session of the 121st Legislature. The Task Force consisted of 8 members, including 4 legislators, and representatives of state, county and municipal law enforcement officers and municipal firefighters.

Problems presented

The Task Force reviewed the variation in retirement and retiree health insurance benefits among law enforcement officers employed by different levels of government, and among local law enforcement officers and firefighters in different municipalities and counties. Task Force members identified the lack of employer-paid retiree health insurance at the local level as the most significant deterrent to recruitment and retention of new law enforcement officers and firefighters. The cost of retiree health insurance may also cause some officers and firefighters to continue working after they are eligible to retire because they cannot afford to pay for retiree health insurance.

The lack of portability of retirement benefits in certain situations may result in lower retirement benefits for job-changers, or may deter people from changing jobs. Retirement benefits are portable for people who move among municipal and county employers in the Maine State Retirement System Consolidated Plan, but are not portable in other situations.

Consideration of a uniform retirement plan

As required by its implementing legislation, the Task Force reviewed the uniform retirement plan for New Hampshire state and local employees. That plan provides for higher benefits than most Maine plans, and is portable because it covers all local and state law enforcement officers and firefighters in a single plan. However, given the cost and administrative difficulties of implementing a uniform plan, the Task Force did not pursue creation of a New-Hampshire-type plan for Maine law enforcement officers and firefighters.

Recommendations:

To address equality and portability problems, the Task Force recommends:

Retiree Health Insurance

- That the State pay a subsidy toward the cost of health insurance for retired county and municipal law enforcement officers and municipal firefighters who retire from certain Maine State Retirement System plans. Current and future retirees would be eligible for the subsidy, which would pay 100% of the cost of retiree coverage, up to a maximum of the amount paid for state retiree health insurance coverage. Law enforcement officers would be eligible for the subsidy if they are retired from a MSRS plan that provides a retirement benefit at least as favorable as 50% of average final compensation after 25 years of service;

- That the subsidy be funded by employee contributions (1.5% of compensation for active law enforcement officers and firefighters who participate in plans that qualify for the subsidy), as well as by a tax on premiums paid for certain types of property and casualty insurance, including commercial and private auto insurance, and commercial and homeowner multiple peril insurance (1/2 of 1% of premium);

- That the Bureau of Insurance develop options for collecting contributions toward the subsidy from businesses that do not pay premiums for coverage of the types of risks covered by auto insurance, and property-related insurance. Options might include a tax on imputed premium, or a tax on the value of certain property; and

Portability of Retirement Benefits

- That state and local law enforcement officers and firefighters who move among certain MSRS-administered retirement plans be given the option of purchasing full or partial portability when they move to a retirement plan that does not otherwise provide for portability.

The Task Force report includes recommended legislation to implement these recommendations.

I. INTRODUCTION

The Task Force to Study Parity and Portability of Retirement Benefits for State Law Enforcement Officers, Municipal and County Law Enforcement Officers and Firefighters was created by Resolve 2003, chapter 76 in the 1st Regular Session of the 121st Legislature. The Task Force consisted of the following 8 members: 2 Senators, 2 members of the House of Representatives, and representatives, one each, of state, county and municipal law enforcement officers and municipal firefighters.

The Task Force was directed to review the differences in retirement benefits provided to law enforcement officers employed by different levels of government, develop options for providing parity and increasing portability of retirement benefits for officers moving among levels of government and among municipalities, to review differences in retirement and health benefits for municipal law enforcement officers and firefighters in different municipalities and consider creation of a uniform retirement and health insurance benefit for those municipal employees.

The Task Force first met during the 2003 interim, and received permission from the Legislative Council to continue its work in the 2004 interim. The Task Force met in 2003 on November 10th, and in 2004 on January 6th, January 26th, August 11th, September 29th and November 12th.

Task Force members invited the following to provide information regarding the study topics: Mike Burke, District Manager, U.S. Social Security Administration; David Barrett, Manager of Personnel Services and Labor Relations for Maine Municipal Association; Gail Drake Wright, Chief Deputy Director of the Maine State Retirement System; Kathy Morin, Assistant to the Chief Deputy Director of the Maine State Retirement System; and Frank Johnson, Executive Director, Division of Employee Health and Benefits, Department of Administrative and Financial Services.

II. BACKGROUND

A. Statement of the problem

Retirement benefits and retiree health insurance benefits for law enforcement officers and firefighters vary greatly among the different levels of government in Maine, and among municipalities. Local[1] law enforcement officers and firefighters usually have less generous retirement benefit packages than those provided to State law enforcement officers in Maine and to state and local law enforcement officers in New Hampshire.[2] Lack of employer-paid retiree health insurance for local law enforcement officers and firefighters is especially significant.

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[1] As used in this report, "local" includes municipal and county.

[2] Some municipalities provide retirement plans for law enforcement officers and firefighters that are at least as generous as State law enforcement officer plans, and possibly more generous. For example, Special Plan #3 provides for payment of 2/3 of AFC after 25 years of service, a higher benefit than the State Police plan of 50% after 25 years.

The inequality of retirement benefits makes it difficult to recruit and retain local law enforcement officers, according to Task Force members, who cited examples of losing municipal police officers to the State Police and to other states with more generous retirement benefits. They also cited examples of difficulty in filling vacant positions. Kevin Joyce, the Task Force member representing county law enforcement officers, reported that it took 2 months to fill 2 vacant positions in the Cumberland County Sheriff's Office, and he cited lack of employer-paid retiree health insurance as a major stumbling block to recruitment.

Lack of employer-paid retiree health insurance for local law enforcement officers may also lead some to continue working past the time they become eligible to retire, in order to continue to receive health insurance coverage at an affordable cost. Paying the full cost of retiree health insurance, say Task Force members, can easily consume a major portion of a person's monthly retirement benefit.

Lack of portability of retirement service credits also discourages law enforcement officers and firefighters from changing employers. This is true of changes between state and local employment, but also changes among municipalities with different retirement systems that do not provide for portability. The federal windfall elimination provision and government pension offset, both offsets against Social Security, may also discourage movement among jobs.

B. Current benefits offered to law enforcement officers and firefighters

1. Retirement – State Law Enforcement Officers

Retirement plans for state law enforcement officers, including State Police, Game Wardens and Marine Patrol officers, are set by Maine law and administered by the Maine State Retirement System (MSRS).

State law enforcement officers are covered by one of a variety of MSRS plans, depending on job category and date of hire. Most state law enforcement officers are covered by a so-called "special plan," meaning that they can retire earlier, with fewer years of service, and/or with a better benefit, than other state employees. Like other state employees, state law enforcement officers do not participate in Social Security.

The following are <u>examples</u> of retirement plans applicable to state law enforcement officers:

- **State Police hired before 9/16/84** can retire with 20 years of service, at any age, with a benefit of ½ of their average final compensation (AFC), plus 2% of AFC for each year of service in excess of 20.

- **State Police hired on or after 9/16/84** can retire with 25 years of service, at any age, with a benefit of 2% of AFC for each year of service.

- **Officers in the "1998 Special Plan" (including forest rangers and certain corrections system employees)** can retire (1) with 25 years of service, at age 55, with a benefit of 2% of AFC per year, reduced if the person retires before normal retirement age[3]; or (2) with 10 years of service after 6/30/98, at age 55, with a benefit of 2% of AFC for each year of service, reduced if the person retires before age 55.

- **Marine Resources and Game Wardens hired after 8/31/84** can retire with 25 years of service, at any age, with a benefit of 2% for each year of service.

More complete information of MSRS retirement plans applicable to state law enforcement officers is found in Appendix C and D. Appendix C shows the MSRS retirement plans that would apply to a person hired today; Appendix D shows all MSRS plans applicable to state law enforcement officers.

2. Retirement – Local law enforcement officers and firefighters

Municipalities and counties are not limited by Maine statute to specific retirement plans. They can choose any type of retirement plan for their employees, as long as the plan meets the federal legal requirement for a sufficient minimum retirement benefit.[4]

Municipalities are not required to participate in Social Security, but they must provide a retirement plan that yields a retirement benefit comparable to Social Security. Municipalities and counties can opt to have all or some of their employees participate in Social Security by signing a so-called "Section 218 agreement," specifying which employees are covered. They can also offer defined benefit plans administered by the MSRS or by others, defined contribution plans, a combination of such plans or a combination of Social Security and other plans.

Because there is no central source of detailed information on the benefits provided by municipalities and counties, the Task Force was not able to gather data on the complete retirement packages offered to law enforcement officers and firefighters by each local government. The Task Force focused on information about the counties and municipalities that participate in the MSRS Consolidated Plan. The information may not present a complete picture[5], but provides useful insight.

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[3] In some cases, the retirement benefit is calculated as a split benefit, and the normal retirement age (NRA) for the pre-1998 service may be the NRA for a Regular MSRS plan (age 60 or 62), rather than 55.

[4] Federal law requires public employers to participate in Social Security, unless they can demonstrate that their alternative plans provide benefits comparable to the benefit provided by Social Security. 26 USC §3121(b)(7)(F). 26 CFR 31.3121(b)(7)-2.

[5] The information provided by the MSRS does not indicate whether the municipality offers supplemental retirement programs, such as deferred compensation plans (457 plans). It specifies which municipalities have signed a "Section 218" agreement to allow some employees to participate in Social Security, but it does not indicate whether the agreement grants that option to law enforcement officers or firefighters. Finally, the MSRS is not able to determine for all municipalities whether employees covered by a Regular Plan are law enforcement officers or firefighters.

The MSRS makes available 11 retirement plans[6] that a municipality or county might offer to law enforcement officers or firefighters: 3 Regular Plans and 8 Special Plans. The following chart explains the basic provisions of those plans. Additional information is provided in Appendix E, which describes the plans, and Appendix F, which lists specific municipalities and counties and which MSRS plan they offer to employees.

Maine State Retirement System
Options within the Consolidated Plan for Participating Local Districts

MSRS Plan	Requirement for Eligibility to Retire	Benefit Provided
Regular Plan A	Age 60; or 25 years of service with a reduced benefit for retiring before age 60	(2% of AFC) x (Years of Service) with or without a cost-of-living adjustment
Regular Plan B	Age 60; or 25 years of service with a reduced benefit for retiring before age 60	(1% of AFC) x (Years of Service) with a cost-of-living adjustment
Special Plan #1	20 years of service, at any age	½ of AFC plus 2% of AFC per year in excess of 20, with or without a COLA
Special Plan #2	25 years of service, at any age	½ of AFC plus 2% of AFC per year in excess of 25, with or without a COLA
Special Plan #3	25 years of service, at any age	2/3 of AFC plus 2% of AFC per year in excess of 25, with or without a COLA
Special Plan #4	Age 55 and 25 years of service	(2% of AFC) x (Years of Service), with or without a COLA

According to the MSRS, there are currently more than 2,100 municipal and county law enforcement officers and municipal firefighters participating in these MSRS retirement plans. An exact number is difficult to obtain because, in some situations, municipalities do not provide a specific code for each covered employee, and law enforcement officers and firefighters may participate in the same plans as other employees. The following information summarizes the prevalence of MSRS retirement plans for new hires in counties and municipalities.

[6] The plans described in this report are plans within the Participating Local District (PLD) Consolidated Plan. Some municipalities and counties have individual MSRS plans, but most are in the Consolidated Plan.

County law enforcement

- 13 of 16 counties in Maine offer MSRS retirement plans to their law enforcement employees (sheriffs and deputy sheriffs).
    - 5 offer a Special Plan
    - 8 offer a Regular Plan
- Knox, Franklin and Somerset counties do not participate in MSRS plans for new hires.

Municipal law enforcement

- Maine has 116 municipal police departments[7] and 2 tribal police departments.
- 81 of the 116 municipal police departments offer MSRS plans.
    - 41 offer a Special Plan
    - 40 offer a Regular Plan
- Most of the larger police departments in the State – those with more than 40 full-time officers[8] – offer Special Plan #2, which provides for retirement after 25 years of service, at any age, with a benefit of ½ of average final compensation.

Municipal firefighters

- Most Maine communities have all-volunteer firefighting departments, and do not provide retirement benefits to volunteers.
- Approximately 64 communities have fire departments containing one or more career firefighters[9]. All but 18 participate in one of the MSRS retirement plans.
- 7 of the 8 municipalities with all-career or mostly-career firefighting departments participate in MSRS retirement plans.
    - Portland, Augusta, Auburn, Brunswick and Old Town cover their career firefighters under Special Plan #2, with all but Old Town providing for cost-of-living adjustments.
    - Gardiner offers Special Plan #3 without cost-of-living adjustments.
    - Lewiston provides Regular Plan A with cost-of-living adjustments.
    - Bangor has a non-MSRS retirement plan, but has some grandfathered firefighters and law enforcement officers in Special Plan #2.
- 38 of the 56 communities with mostly-volunteer fire departments offer MSRS retirement plans to their career firefighters.
    - 20 communities participate in Regular MSRS Plans.
    - 18 are in special plans, about evenly divided between Special Plans #2, 3 and 4.

The list above summarizes the MSRS plans that apply to new hires. Some municipalities and counties that have withdrawn from the MSRS have employees who continue to participate as grandfathered employees in MSRS plans. Some municipalities and

[7] Based on information provided by the Maine Chiefs of Police Association
[8] Based on the Full-Time Officer Report, Maine Criminal Justice Academy.
[9] Based on information provided by the Office of the State Fire Marshal

counties remain within the MSRS, but have different plans for employees hired before a certain date than for employees hired after a certain date.

3. Retiree Health Insurance -- State law enforcement officers

State law enforcement officers are generally eligible for 100% state-paid retiree health insurance as long as they meet the eligibility criteria applicable to all state employees: i.e., they must have participated in the state health insurance plan for at least one year prior to retiring and must be drawing a retirement benefit from the MSRS.

In some cases, the State pays less than 100% of the cost of the retiree's coverage. If a person was first hired after July 1, 1991 and participates in the state health plan for fewer than 5 years before retirement, the person may participate in the state health insurance plan after retirement, but the State makes no contribution toward the premium. With 5 years of participation, the State pays 50% of the premium for retiree coverage, at 6 years, 60% and so on until at 10 years, the State pays the full cost of retiree coverage.

State retirees who are not yet eligible for Medicare are enrolled in the same group health insurance plan as active state employees, which is currently an Anthem HMO Choice plan. Medicare-eligible employees have a Group Companion Plan that supplements Medicare Parts A and B.

4. Retiree Health Insurance -- Municipal firefighters and municipal and county law enforcement officers

Municipalities and counties are not required to provide health insurance to their active or retired law enforcement officers and firefighters. However, if they provide health insurance to active police officers, they must allow those officers to participate in the group plan after they retire.[10] The municipality or county is not required to contribute toward the premium cost.

Municipalities and counties insure their active law enforcement officers and firefighters through a variety of sources, including union-sponsored plans and the Maine Municipal Employee Health Trust (MMEHT), operated by the Maine Municipal Association. MMEHT is a self-funded pool that offers health, dental, life and disability insurance to local governments. The trust offers 5 different health insurance plans, and local units of government may elect to offer one of the plans to their employees. The cost of the plans varies, and employer contribution toward the cost is determined at the local level. MMA does not collect data on payment of premium by employers.

According to a MMEHT Census dated December, 2003, 264 municipalities and 10 counties participate in the MMEHT, including Auburn, Augusta, South Portland, Westbrook, Cumberland County, Kennebec County and others.

[10] 30-A MRSA §2677

C. Impact on retirement benefits of changing jobs

When retirement plans differ from employer to employer, a person who changes jobs may end up with a less generous retirement package than if he or she had not changed jobs. This occurs when the retirement plan to which he or she moves does not provide for portability. Portability is the ability to carry retirement benefits from one retirement plan to another.

When benefits are not portable, a person's eligibility to retire and retirement benefit are determined under each of his employer's retirement plans based on the number of years and compensation earned as a member of that retirement plan, without regard to other years or compensation.

Retirement benefits are not portable between State retirement plans and Consolidated Plan participating local district (PLD) plans, so a person who moves from a position of police officer in a municipality that participates in the Consolidated Plan to a position with the State Police might have a benefit calculated as follows.

1. Example of the Impact of a Job Change on a Person's Retirement Benefit, without Portability

Employee retires at age 53 after 30 years of service as a law enforcement officer (15 years of service as a Municipal Police Officer in MSRS Special Plan #2, followed by 15 years as a State Police Officer). Assume the employee's Average Final Compensation (AFC) was $35,000 as a municipal police officer and $52,000 as a State Police Officer.

This person did not meet the eligibility requirement for **either** of the Special Plans in which he participated (MSRS Special Plan #2 for PLDs and the State Police Special Plan). Therefore, his eligibility to retire and his retirement benefit are determined under the Regular PLD Plan and the Regular State Employee Plan, as follows:

Regular Municipal (PLD) Plan

(2% of AFC) x (15 years),
Reduced by approx. 15% because of early retirement[11] = approx. $8,925

Regular State Employee Plan

(2% of AFC) x (15 years)
Reduced by approx. 15% because of early retirement[12] = $13,260

[11] Normal retirement age for the Regular PLD plan is 60, and a person's benefit is reduced by approximately 2-1/8% for each year prior to normal retirement age. He is retiring 7 years before NRA, so the reduction is approximately 15%.

[12] This calculation assumes that the person is a "pre-cliff" employee, i.e., he had 10 years of service as of July 1, 1993, so his normal retirement age is 60. Otherwise, his normal retirement age is 62 and he is retiring 9 years before NRA, and his benefit would be reduced by 6% for each year before NRA, for a total reduction of 63%.

Total annual benefit calculated as a split benefit
$13,260 + $8,925 = $22,185

If the employee had remained a municipal police officer in the same retirement plan for 30 years, instead of changing jobs, his annual benefit might have been as follows: (2% of AFC) x (30 years) = $31,200, or $9,015 higher than under the previous scenario, assuming that his AFC rose to $52,000. The higher benefit results from 2 factors. First, the employee would have qualified to retire under the PLD Special Plan because he had more than 25 years of service. As a retiree from Special Plan #2, he would not have suffered a reduction of his benefit due to early retirement, because a person can retire from Special Plan #2 at any age, as long as he has 25 years of service. In addition, the higher compensation earned in the later years of his career would be used in calculating the benefit for all his years of service, not just for his later years. Even if the employee's average final compensation had not risen as high as $52,000, his final benefit would still likely be higher than the split benefit calculated in the previous example.

2. Types of portability

The employee described above, who changed employers, would have had a different benefit calculation if the retirement plan to which he moved provided for portability. The impact of portability would depend on the type of portability provided by the plan to which he moved after the job change. The following describes various aspects of portability.

(a) Eligibility to retire

Portability may allow a person to count years of service earned in an earlier retirement plan toward the number of years required for eligibility to retire from a later plan. Earlier service years may count on a one-for-one basis or on a percentage-basis. If years counted one-for-one, the person in the example above would have been able to count his 15 years as a municipal police officer toward the years-of-service requirement to retire as a State Police Officer (25 years). He would have been able to retire 5 years earlier, and his benefit from the State Police would have been calculated under the State Police Special Plan, without a reduction for early retirement (because there is no age requirement for State Police). As an alternative, years may also be converted into equivalent years, such as providing that each 3 years of service in a less valuable plan equals 2 years in a more valuable plan, for purposes of determining eligibility to retire.

(b) Calculation of the Benefit

Average final compensation

Portability may also allow a person to take the highest 3 years of compensation with either employer in determining average final compensation when calculating both parts of his retirement benefit. Assuming that salaries increase later in a person's career, the ability to consider all years of compensation would result in a higher AFC than if only compensation from each employer were considered in calculating the AFC applicable to those years of service.

(c) Calculation of the Benefit
Split benefit calculation or Single calculation
Years of service earned within a plan that provides for a less generous benefit, such as a Regular Plan, are of less value in producing a retirement benefit than years of service earned in a more generous plan, such as a Special Plan. So, when a person moves from a Regular Plan to a Special Plan, either the benefit is calculated in pieces, as a split benefit, or some adjustment is made to account for the difference in value of the years. For example, 12 years of service earned in Regular Plan A is, by statute, converted into 8 years in Special Plan #2. The benefit is then calculated in a single step, using the 8 years as the years of service component in the formula.

The chart in Appendix G provides additional information, including examples of MSRS retirement plans that provide for one or more types of portability.

3. Impact on Retiree Health Insurance of changing jobs
For a person who retires from an employer that provides retiree health insurance, changing jobs does not usually have an impact on retiree health insurance. Portability is usually not an issue when it comes to retiree health insurance, because the employee's years of service is not relevant to the amount of the benefit.

However, for a person who retires from state employment, the number of years of service matters in 2 situations.

First, if the person was first hired by the State after July 1, 1991, and has fewer than 10 years of participation in the group health plan, the State pays less than 100% of the cost of retiree coverage. With fewer than 5 years of participation in the group health plan, the person may participate in the group plan after retirement, but the State makes no contribution toward the cost. With 5 years of participation, the State pays 50% of the retiree cost, at 6 years, 60% and so on until, at 10 years, the State pays the full cost of retiree coverage.

Second, if a person leaves State employment before beginning to draw his MSRS benefit, the person is eligible to participate in the health insurance program at retirement only if that person had 25 years of service at the time he left state employment and meets one of 3 additional criteria set forth in the statute.[13]

4. Impact of job change on Social Security
Federal Social Security law may also deter movement between jobs. A person who moves between a job covered by Social Security and a job covered by the MSRS or other government pension program in lieu of Social Security, and who has earned a retirement benefit from both programs, often suffers a reduction in his or her Social Security benefit.

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[13] 5 MRSA §285. The person must either pay the cost of coverage until retirement, demonstrate continuing coverage under a different health insurance plan prior to retirement, or elect at retirement to rejoin the plan and be subject to possible pre-existing condition exclusions.

This reduction is referred to as the "Social Security Offset." It results from a provision of federal law known as the "Windfall Elimination Provision" or "WEP." The WEP is intended to ensure that the person's Social Security benefit is calculated in a way that more accurately represents the person's earnings.

The Social Security program is designed so that lower-wage workers receive a higher proportion of their average wage as a benefit than average-wage or higher-wage workers. The formula for a Social Security benefit for a person retiring in 2005[14] is:

> <u>90%</u> of the first $627 of the person's average monthly earnings[15], PLUS
> 32% of the amount from $628 to $3,779, PLUS
> 15% of the remainder.

The calculation assumes that the average earnings figure is an accurate reflection of the person's earnings during his or her lifetime. But if a person has worked the majority of his or her career in government employment, and fewer than 30 years in a career covered by Social Security, the normal calculation underestimates the person's earnings. So the WEP recalculates the benefit as follows:

> <u>40%</u> of the first $627 of average earnings, PLUS
> 32% of the amount from $628 to $3,779, PLUS
> 15% of the remainder

A second type of Social Security offset known as the "Government Pension Offset," or "GPO," reduces the Social Security survivor benefit payable to a surviving spouse who also receives a government pension. That offset reduces the survivor benefit by 1/3.

The offsets do not occur if the person receiving both types of pension income had 30 years of substantial Social-Security-covered employment, either because he participated in Social Security in addition to his government retirement plan or because he was only covered by Social Security. The offsets would be lower if the person had at least 21 years of substantial Social Security earnings.

Following enactment of the offsets and other changes in federal Social Security law in 1983, Maine policymakers in the late 1980's and early 1990's examined the impact of these federal law changes on state employees and considered[16] whether to move state employees onto Social Security, or a combination of Social Security and a smaller state retirement plan, but to date have not adopted such a plan.

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[14] The percentages used in the formula (90%, 32% and 15%) remain constant from year to year, but the dollar thresholds for each percentage are adjusted annually based on changes in the average wage.

[15] The calculation of a person's average monthly earnings is based on 35 years of employment, with employment not covered by Social Security counted as zero earnings employment, and is indexed to wage growth.

[16] See the 1987 and 1988 reports of the Commission to Study the Integration of the Maine State Retirement System with Social Security created by Resolves 1987, chapter 53; the 1988 report of the Committee to Study the Retirement System created by PL 1987, chapter 68, chaired by Robert Monks (the "Monks 1" report) and the 1994 report of the Committee to Study the Retirement System, created by PL 1993, chapter 410 ("Monks 2").

D. New Hampshire Uniform Retirement Plan

Once fully implemented, a uniform retirement plan for all state and local law enforcement officers and firefighters would eliminate concerns about portability and parity. The Task Force gathered information about New Hampshire's retirement system, as an example of such a uniform plan.

Since the 1960's, New Hampshire has had a single retirement plan for all state and local law enforcement officers and firefighters[17]. The following is an outline of the New Hampshire Retirement System (NHRS), as it applies to those employees, known in the New Hampshire system as "Group II employees." These employees do not participate in Social Security.

- Eligibility to Retire
  Age 45 with 20 years of service OR age 60, regardless of service

- Benefit Amount
  2.5% of average final compensation for each year of service within the plan

- Employer contribution
  The employer contribution is determined by the NHRS on the basis of actuarial analysis. In 2004, the employer contribution was 12.11% of compensation for law enforcement officers and 20.68% for firefighters. The State of New Hampshire pays 35% of the local employer's contribution for law enforcement officers and firefighters.

- Employee contribution
  The employee contribution is set by statute at 9.3% of compensation for Group II employees

- Retiree Health Insurance
  The NHRS provides a medical subsidy of a fixed amount to Group II retirees who were members or retirees as of 6/30/00. The 2004 subsidy for persons under the age of 65 is $298.13 per month for an individual, and double that amount for a retiree & spouse. When they reach 65, Medicare becomes the primary coverage, and the subsidy pays $188.02 per person per month toward a Medicare supplement policy. The policies are provided through the former local government employer. The subsidy is paid to the former employer, and any additional cost above the subsidy must be paid either by the employee or the employer. New Hampshire law allows an 8% increase in the subsidy amount each July 1. The subsidy is funded by a special account, created from actuarially calculated gains of more than a half percent above the retirement Trust Fund's, assumed rate of return. In fiscal year 2002-03, $5.669

[17] The NHRS also covers teachers, state employees and other municipal employees (if the municipal employer elects to participate). This summary only relates, however, to the LEO and FF part of the NHRS.

million was paid in subsidies for police officers, and $3.327 million was paid for firefighters.

III. TASK FORCE DISCUSSIONS

The Task Force began its work by examining the different retirement packages currently offered to state, county and municipal law enforcement officers and to municipal firefighters, and by learning about portability among MSRS plans. At their first meeting, members brainstormed about possible alternatives to the current system, including:

- Creation of a mandatory uniform retirement plan like that offered in New Hampshire, either restricted to new hires or for all law enforcement officers and firefighters;

- Establishment of a minimum retirement benefit package that exceeds the Social Security minimum, to be offered by all municipalities to police officers and firefighters, and allowing for variation among municipalities that wish to exceed the minimum; and

- Allowing individual employees to "buy in" to a better retirement plan or to retiree health insurance when they would not otherwise qualify for those benefits, either by paying their own costs or by negotiating for their employer to pay the additional cost.

Discussions at early meetings also brought forth a number of concerns about changing from the current system, including:

- Additional cost incurred to improve benefits, and whether the additional cost would be borne by the municipality or the State;

- The administrative complexity of creating a new uniform retirement plan and moving existing employees onto that plan;

- The inequity of creating a plan that only new hires can participate in, leaving existing employees with less favorable plans;

- The difficulty of maintaining uniformity among plans, when groups of employees can request improvements from later Legislatures; and

- The difficulty of narrowing down all current options available to municipalities to a small number of plans, or a single plan.

For its 2nd meeting, the Task Force asked a representative of the Maine Municipal Association (MMA) to attend to answer questions and provide comments to assist the Task Force in its deliberations. David Barrett, Manager of Personnel Services and Labor Relations for MMA explained that the current variation in retirement benefits among municipalities is the result of years of negotiations between employers and employees. A uniform, state-determined retirement package would replace that process, and reduce the flexibility that employees now have during negotiations. In response to a question from a Task Force member, Mr. Barrett reported that portability of retirement benefits seems to concern employees less than in the past, because the Consolidated Plan provides portability. Employees are more concerned, he said, about other benefits, especially health insurance.

Retiree health insurance

At their 3rd and 4th Task Force meetings, members focused on retiree health insurance. Frank Johnson, Executive Director of Employee Health and Benefits Division of the Department of Administrative and Financial Services, explained the state employee health plan and the requirements for eligibility for retirees. Some Task Force members believed that a person moving to state employment from municipal employment would be required to work for the state for 25 years in order to participate in the state retiree health insurance program. Based on this belief, they wanted to amend the law to allow such employees to buy their way into retiree health insurance. However, as Mr. Johnson explained, a state employee hired after 7/1/91 need only participate in the state employee health plan for 5 years before retirement in order to have some level of State contribution toward the cost of the insurance. A state employee need only participate in the plan for 10 years prior to retirement to earn state payment of 100% of the retiree's premium. Following this explanation, members did not pursue the option of "buying into" the state health insurance plan.

Task Force members also discussed whether to have all municipal law enforcement officers and firefighters participate in the state employee health insurance plan when they retire. But given administrative difficulties with such a program, members instead pursued the less complex option of providing a state subsidy toward the cost of retiree health insurance, similar to the subsidy provided to teachers. Municipal and county law enforcement officers and municipal firefighters, upon retirement, would continue to participate in whatever group plan their employer provided for active employees and the State would pay a certain percentage of the cost of that plan. The Task Force continued to pursue this option during subsequent meetings.

Targeting the Health insurance subsidy

Task Force members believed that a retiree health insurance subsidy should accomplish two goals: (1) provide assistance to individual retirees; and (2) by limiting the subsidy to municipalities that participate in MSRS retirement plans providing a certain level of benefit, to provide incentive to municipalities to move into such plans, if they are not already participating. Municipalities would have incentive to move to those MSRS retirement plans because they would be able to offer retiree health insurance as a recruitment and retention tool with the State covering some or all of the cost of the benefit.

After reviewing information on participation in MSRS Special Plans, members concluded that the majority of local law enforcement officers and firefighters are already covered by MSRS Consolidated Plan Special Plan #2, which provides for retirement after 25 years of service, at any age, with a benefit of 50% of average final compensation (plus 2% for each year beyond 25). Members proposed to link the health insurance subsidy to provision of a retirement plan that meets or exceeds Special Plan #2. Members referred to such plans as "25/50 or better" plans.

The category includes Special Plan #2 with a cost-of-living adjustment (COLA), and Special Plans #1 and #3 with or without COLA.

At the request of the Task Force, Frank Johnson provided a rough estimate of the cost of a 40% subsidy, similar to that currently provided to retired teachers, to local law enforcement officers and firefighters in "25/50 or better" retirement plans. Based on a rough, non-actuarial calculation by Mr. Johnson and by Task Force staff:

- The cost of a 40% subsidy applicable only to persons who retire after the law passes (based on 1,524 law enforcement officers and firefighters currently participating in 25/50 or better plans) might range from $3.8 to $4.1 million annually.

- If the 40% subsidy began immediately and included all current and future retirees, based on the number of current law enforcement officer and firefighter retirees in 25/50 or better plans (1,033) and assuming 40 additional retirees per year, the cost might range from $2.2 million to $2.8 million in the first year, increasing by between $83,000 and $109,800 per year.

- The cost of a 100% subsidy for all current and future retirees might range from $5.4 million to $7 million in the first year, increasing by from $208,000 to $272,000 each year after the first year.

Appendix H describes the methodology for these estimates, which are rough estimates calculated without actuarial analysis.

Possible sources of revenue for the subsidy
Task Force members discussed possible sources of revenue to pay for the subsidy, including the insurance premium tax,[18] a tax similar to the fire investigation and prevention tax[19] and a surcharge on fines imposed for certain criminal convictions.

The insurance premium tax is imposed on all insurance policy premiums paid in Maine, at a rate of 1% for long-term care policies and 2% for most other types of insurance. Collections from the insurance premium tax go into the State General Fund. Companies that self-insure do not pay the tax.

The Fire Investigation and Prevention Tax is imposed only on premiums attributable to fire risks. The general rate is 1.4% of premium, but special additional assessments have been made in fiscal years 2002 and 2003. This tax funds fire prevention, investigation and public education activities of the Department of Public Safety, as well as defraying the cost of fire training and education programs in the Community College System. According to Task Force members, the rationale for charging the costs of such programs to insurance policies relating to fire risk is that insurers and insured property benefit from training and prevention programs, and should therefore bear part of the cost for such programs.

[18] 36 MRSA c. 357
[19] 25 MRSA §2399

With regard to taxation of insurance premiums to pay for law enforcement officer and firefighter programs, Task Force members considered creating a different premium tax that would have broader application than the Fire Investigation and Prevention Tax, but would not apply to all insurance policies.

Members also considered a surcharge on fines imposed by courts when a person is convicted of certain types of crimes, such as drug-related crimes or felonies (Class A, B, or C crimes).

Portability and its cost

Since Task Force members did not pursue the idea of a mandatory uniform retirement plan for all law enforcement officers and firefighters, portability of benefits remained an issue. At their 5th meeting, members were briefed on portability concepts by Kathy Morin of the MSRS.

As described in the background section of this report, a person who moves among plans in the Consolidated Plan for Participating Local Districts can take all or part of the benefit of his earlier years of service with him when he moves from one employer in that Plan to another. But there is no portability for someone moving between State employment and municipal or county employment or someone moving among and between municipalities and counties that do not both participate in the Consolidated Plan.

Adding portability to a retirement plan adds cost. First, when a person moves from an employer with a less favorable plan to an employer with a more favorable plan (e.g., from a plan that requires 25 years of service to one that requires 20 years), the new employer could be required to pay a benefit for which insufficient funds have been set aside. An employer that has 25 years to save for a benefit can put aside less each year than an employer saving to pay a benefit in 20 years because, among other things, the 25-year employer is likely to have 5 more years of contributions as well as 5 more years of investment earnings to rely on for funding the benefit. Even if the employer and employee contributions from the first employer are transferred to the 2nd employer, there is not enough to fund the better benefit.

Second, a person whose retirement benefit is portable is more likely to qualify for a Special Plan benefit -- a more valuable and costly benefit -- than a person whose benefit is not portable and therefore qualifies only for a Regular Plan benefit. Special Plans usually require 20 or 25 years of service before a person is eligible to retire from that plan. A person in the Special Plan can retire without meeting that years-of-service requirement, but he will be treated at retirement as if he were in a Regular retirement plan; his benefit will be reduced if he has not reached the normal retirement age of that Regular Plan (usually age 60 or 62). Allowing portability would increase the chances that a person will qualify for the Special Plan benefit with his or her last employer, without reduction based on early retirement, since Special Plans have either no age requirement or a lower age requirement than the Regular Plans.

A cost for portability may also be incurred by the 1st employer, because the employee contributions, interest and possibly the employer contributions attributable to that employee are transferred out of employer #1's fund and the funds are unavailable to cover the cost of retirement benefits for employees who remain in the plan. Normally, when actuaries determine how much money the employer needs to contribute to the plan, there is an assumption that some people will leave the plan and will not be entitled to a benefit, so the employer contributions set aside for that person remain in the plan and become available to fund other benefits. Allowing more people to transfer funds to other plans takes away that ability.

The costs of portability in the Consolidated Plan are currently spread out among all employers in the Plan. When the actuaries determine the required employer contribution, they assume that some level of costs will be imposed on the new and old employers, so the rates paid by all employers provide a cushion to cover those costs. In addition, the rules for portability among those plans provide that a person does not necessarily gain the full benefit of prior years of service, e.g., a person gets 1 year of credit in Special Plan #1 for each 2 years of service in a Regular Plan. This reduces the cost somewhat, while giving the employee some benefit from his prior years of service

Task Force members acknowledged the additional costs, and decided that they did not want to impose those additional costs on employers. Instead, they proposed that the employee be given the option to purchase full or partial portability. The Retirement System can determine the actuarial cost of portability. While the cost may be significant in some cases, e.g., when an employee is nearing retirement age, Task Force members wanted employees to have the option. Buying in to a better retirement benefit may provide a more certain long-term benefit than making investments on one's own.

IV. RECOMMENDATIONS

The Task Force voted unanimously[20] to recommend the following actions to the Legislature. Legislation to implement the recommendations is included as Appendix J.

Retiree Health Insurance

<u>The Task Force recommends</u>:

- That the State pay a subsidy toward the cost of health insurance for retired county and municipal law enforcement officers and municipal firefighters who retire from certain Maine State Retirement System plans. Current and future retirees would be eligible for the subsidy, which would pay 100% of the cost of retiree coverage, up to a maximum of the amount paid for state retiree health insurance coverage. Law enforcement officers would be eligible for the subsidy if they are retired from a MSRS plan that provides a retirement benefit at least as favorable as 50% of average final compensation after 25 years of service;

- That the subsidy be funded by employee contributions (1.5% of compensation for active law enforcement officers and firefighters who participate in plans that qualify for the

[20] Senator Blais was not present at the final meeting of the Task Force, and did not participate in the vote on recommendations.

subsidy), as well as by a tax on premiums paid for certain types of property and casualty insurance, including commercial and private auto insurance, and commercial and homeowner multiple peril insurance (1/2 of 1% of premium); and

- That the Bureau of Insurance develop options for collecting contributions toward the subsidy from businesses that do not pay premiums for coverage of the types of risks covered by auto insurance, and property-related insurance. Options might include a tax on imputed premium, or a tax on the value of certain property.

Task Force members representing municipal and county law enforcement officers said that the lack of employer-paid retiree health insurance as part of an employee's benefit package is a significant deterrent to hiring and retaining law enforcement officers, perhaps more significant than the retirement benefit plan itself. There is a precedent for State payment of retiree health insurance premiums for certain local employees, since the state currently pays 40% of a retired teacher's health insurance premium. The subsidy for law enforcement officers and firefighters could work in much the same way.

The subsidy would be capped at the dollar amount paid as premium for retired State employees with similar plans, i.e., for a Medicare-eligible retiree, the dollar amount would be the amount paid by the State for a Medicare Supplement policy. A retiree is eligible for the subsidy whether his insurance is provided through the former employer's plan, or, if he is not able to participate in the employer's plan, through another group or individual plan.

The Task Force proposes that the subsidy be funded from 2 sources: active employees who are likely to benefit from the subsidy when they retire, and insurance policies that cover losses that might involve police or firefighters, such as insurance covering auto accidents, fires, and other accidents and losses.

Task Force members representing local law enforcement officers expressed the belief that active law enforcement officers and firefighters would be willing to share in the cost of such a benefit, and that paying an additional 1.5% of compensation would make their total contribution toward a package of retirement benefits comparable to that paid by State Police Officers for their retirement plan.[21]

The employee contribution would be made to a pooled account dedicated to paying for the subsidy. Active employees would not have a right to a refund of any contributions made for this purpose; all funds would be used to pay the subsidy for all those who become entitled to it.

The other source of funds would be a tax on the premiums paid for certain types of property and casualty insurance. There is precedent for taxing insurance premiums to cover public safety programs. The Fire Investigation and Prevention Tax is levied against premiums paid to cover fire risks; revenue from the tax funds firefighter training and activities of the Department of

[21] State Police currently pay 8.65% of compensation toward their retirement benefit for the first 25 years of service, and 7.65% thereafter. State Police do not make a contribution to pay for retiree health insurance. That cost is paid from the State General Fund, Highway Fund or other accounts.

Public Safety relating to public education, prevention and investigation of fires. The Task Force recommendation would create a separate tax that applies more broadly to all types of insurance that cover risks that might involve police or firefighting services, including auto insurance, homeowners insurance, commercial risks, and others. It would not apply to health and life insurance, or similar types of insurance.

Finally, the Task Force believes that businesses that do not have insurance policies for the types of risks described above should pay a fair share of the costs of the subsidy. Since they do not pay insurance premiums, they should be assessed on some other basis. An example of an alternative assessment provision is found in the workers' compensation law. Under that law, self-insured employers are assessed to cover administrative costs of the workers' compensation system on the basis of aggregate workers' compensation benefits paid, rather than on the basis of premiums paid. The Task Force did not have sufficient time to develop a method of assessing businesses that do not have insurance coverage for fire, accident and the other types of property and casualty insurance noted above. Instead, the Task Force recommends that the Bureau of Insurance develop and report some options for assessment to the Legislature.

Portability of Retirement Benefits

The Task Force recommends:

- That state and local law enforcement officers and firefighters who move among certain MSRS-administered retirement plans be given the option of purchasing full or partial portability when they move to a retirement plan that does not otherwise provide for portability.

Current law provides an opportunity for certain MSRS members to improve their retirement benefits, at their own expense, by purchasing service credit for military service, service in the Peace Corps, educational leave, and certain other types of service. This Task Force recommendation adds a similar provision by allowing certain law enforcement officers and firefighters to improve their retirement benefit, at their own expense, by paying the cost of full or partial portability of prior service as a law enforcement officer or firefighter.

This provision would apply only to officers and firefighters moving among state and local retirement plans that provide a benefit of 50% of average final compensation after 25 years of service, or better. A "better" plan would include a plan that provides a benefit of more than 50% of AFC after 25 years of service, and a plan that provides a 50% benefit after fewer than 25 years.

If a person elects to purchase portability, the MSRS would calculate the cost and allow the employee to pay the cost over time or in a single sum, as it currently provides for purchases of service credit. A person who chooses not to purchase portability would have his retirement benefit calculated separately for each plan in which he participated, as provided under current law.

APPENDIX A

Task Force Members

APPENDIX B

Authorizing Legislation

APPENDIX C

MSRS Retirement Plans, New State Law Enforcement Officer Hires

APPENDIX D

All MSRS Retirement Plans Applicable to State Law Enforcement Officers

APPENDIX E

Types of Retirement Plans Covering Municipal and County Law Enforcement Officers and Municipal Firefighters

APPENDIX F

List of MSRS Retirement Plans Offered by Specific Municipalities and Counties

APPENDIX G

Chart Illustrating the Impact of Various Portability Provisions on Retirement Benefits

APPENDIX H

Cost Estimates for Retiree Health Insurance Subsidy

APPENDIX I

Information on Insurance Premium Taxes

APPENDIX J

Draft Legislation