maine PERS Public Employees Retirement System

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Date: April 10, 2018

To: PLD Consolidated Plan Employers

Subject: Proposed Plan Changes

MainePERS has developed seven changes to the Participating Local District Consolidated Retirement Plan (PLD Plan), many of which may affect you as an employer or your employees as members or retirees. These changes are designed to strengthen our ability to provide Plan benefits throughout your participants' retirements and to maintain stable Plan costs in an increasingly challenging financial market environment.

The PLD Plan is currently one of the stronger defined benefit plans in the country. This Plan came through the 2009 recession with an 87% funding level, compared to the national average, which declined to 72%.

Without changes in how the rate structure is managed, however, MainePERS cannot prevent employer rates from climbing in the future to levels that may be unacceptable to you as an employer. This letter explains the framework we have developed to assist us in effectively navigating future financial market volatility while creating the least disruption to your budget management.

Contribution Rate Management

The basis for this framework is a risk-sharing contribution rate structure that maintains the integrity of the benefit but reduces contribution rate uncertainty when the financial markets are volatile. This framework enables MainePERS to keep the contribution rates lower than comparable plans around the country while providing employers and members a stable budgeting framework even through economic disruptions like the 2009 recession or similar, lesser disruptions.

The current rate structure model adjusts employer contributions annually for market and other changes that affect Plan costs, such as mortality or inflation. This structure resulted in a reduction of employer rates to 3% following the financial market run-up that happened in the 1990s. Employer rates were scheduled to begin returning to their normal aggregate 8% level in 2009, which was intended to keep the Plan fully funded, but not overfunded.

The 2009 recession collided with the scheduled return to the original rate structure, frustrating many employers who wondered if there would be an end to rate increases. Our new model for developing rates avoids this situation in the future, providing you with a budgeting framework on which you can rely.

***New* - Variable Contribution Rates with Caps for Employers and Active Members**

Both employer and active member contribution rates will now be adjusted annually. This is a change from fixed rates for employees and variable rates for the employer. Employer contribution rates will be capped at an aggregate of 12.5%, and aggregate contribution rates for active members will be capped at

9%. (Differing options within the PLD Plan have varying costs and rates, some of which will be higher and some of which will be lower than the aggregate cap).

- *Why this change?* Contribution rates change each year for several reasons. One of the most frequent is financial market performance. This change enables both employers and active members to share in both good and poor financial markets without fear of run-away rates.
    - *Important Note* – Cap levels will be re-evaluated in 2021 and every 5 years thereafter to make sure they are consistent with total plan costs for changes in inflation, member lifespans, etc.
- *These changes will be effective July 1, 2018 but will not impact rates until FY2020.*

New - Annual Cost-of-Living-Adjustments (COLA)

If severe market losses create contribution rates that would exceed employer and active member caps, excess required contributions will be smoothed into future COLAs on the same actuarial basis that market losses or gains are smoothed into contribution rates. Market rebounds or recovery will then be smoothed back into future COLAs until eligible members receive the full unreduced COLA, and then smoothed into employer and member rates to reduce those rates below the cap.

- *Why this change?* When severe or extended market downturns occur, contribution rates are automatically increased. Historically in most defined benefit plans, COLAs have also been frozen to reduce the increase in rates and help recover plan funding. The new method enables COLAs to continue to be paid, just at a lower rate than would have otherwise occurred. Avoiding COLA freezes in bad financial markets helps retirees maintain their standard of living while still sharing in market risk.
    - *Important Note* – This substantially reduces the risk of COLA freezes due to prolonged or unexpected market downturns. It cannot eliminate freezes if market losses are excessively severe.
- *These changes will be effective July 1, 2018 but will not impact rates or COLAs until FY2020.*

Non-Core Benefit Changes

The goal of the total set of changes to the Plan is to enable MainePERS to pay the core benefit throughout all participants' retirements. The core benefit is average final compensation multiplied by a factor of 1% or 2% (depending on the specific plan in which a member is enrolled) multiplied by the years of service credit.

There are four changes to retirement benefit provisions that add-on to but do not change the core benefit. These provisions are being updated because they were implemented in earlier times when pension plans could afford to serve multiple purposes. Aligning these with the current pension environment will keep the Plan attractive at an affordable cost.

Unused Sick and/or Vacation

Currently, retiring members are eligible to convert some unused sick and/or vacation accruals to an increase in their retirement benefit. Eligibility is changing from all members to members with 20 or more years of service at retirement.

- *Why this change?* Limiting this costly benefit to career employees reduces overall plan costs while creating an incentive for members to stay in the plan.
- *Effective in early FY2019.*

Early Retirement Subsidy

The early retirement reduction factor is increasing from 2.125% per year for age 60 plan members and 6% per year for age 65 plan members to approximately 6%-7% or less per year for all members based on the number of years a member retires before their normal retirement age.

- *Why this change?* Members that retire early receive a higher lifetime benefit than they otherwise would because they receive additional benefit payments in retirement. The actual cost of these extra payments is approximately 6%-7% of the retiree's normal benefit for each additional year of early retirement. These additional costs are subsidized by all remaining active members and employers through higher contribution rates. This change creates equity between members retiring before and after normal retirement. The actual average reduction for each member will vary based on the number of years of early retirement and may be less than 6%-7%.
- *Effective July 1, 2018.*
    - *Exception* – Age 60 plan members with 20 or more years of PLD service credit as of July 1, 2019 will continue to be eligible for the 2.125% reduction.

Retire/Rehire

PLD employers may continue to hire retirees receiving a PLD Plan retirement benefit. The employer can either: 1) allow the retiree to re-enter the PLD Plan, discontinue their benefit, and earn additional service credit; or 2) pay the unfunded actuarial liability (UAL) portion of current contribution rates on the pay for that position if the rehired PLD Plan retiree continues to receive their MainePERS benefit. The FY2019 UAL rate for any retiree who first returns to work during that year is the "Adjustment to Payroll Rate" on the annual Statement of Consolidated Plan Costs we have already provided to you. The situation a retired member returning to work will have will be dependent on the option their employer offers. This change will not apply to retirees who already have returned to work under an existing employment agreement until the agreement expires or July of 2021, whichever is earlier. It will apply to all new agreements.

- *Why this change*? Retire/rehire without conditions currently reduces contributions to the Plan. This will help control unnecessary contribution rate growth, is cost-neutral to the PLD Plan, and helps keep the PLD Plan strong into the future.
- *Effective July 1, 2018.*

Cost-of-Living-Adjustment (COLA)

The COLA cap will be adjusted to up to 2.5% of the Consumer Price Index for Urban Consumers (CPI-U) with a 2-year waiting period from the current cap of 3% that has a 1-year waiting period.

- *Why this change?* The average CPI-U for the last 30 years was 2.6%, for the last 20 years 2.2%, and for the last 10 years 1.7%. Inflation is anticipated to remain at levels closer to the last twenty years. A COLA cap that reflects inflation helps keep retiree benefits current and keeps plan costs reasonable. The two-year waiting period occurs at the beginning of retirement.

- *The change in the COLA cap is effective July 1, 2018.*
- *The change in the COLA waiting period is effective for those retiring on or after September 1, 2019.*

When are These Changes Effective?

Most changes will be effective July 1, 2018 with the exceptions of the early retirement subsidy reduction and the change in the COLA waiting period, which will be effective July 1, 2019 and September 1, 2019, respectively.

Withdrawal Liability

Changes in the contribution rate framework and benefits were created to protect the PLD Plan benefits that we know you value. They were also created to assist employers in remaining in the plan by creating reasonable and predictable costs.

If you follow the news, you know that several private sector multi-employer plans have reduced their actual benefit levels because they are running out of money in their trust funds, primarily due to employer withdrawals. Federal legislation is being introduced to save these benefits. It is uncertain where that will go. However, what is certain is that the PLD Plan as a local government plan has no option to go elsewhere for funding.

MainePERS is implementing a withdrawal liability payment requirement to further protect the Plan. This means that if an employer decides to withdraw from the PLD Plan, they will be responsible for their share of any remaining unfunded actuarial liability based on their payroll at the time of withdrawal.

This is an equitable solution that enables employers to withdraw without harming the remaining employers and members in the Plan. It is effective for any PLD withdrawing at a time when the Plan is not fully funded.

Rulemaking

These changes will be considered by the MainePERS Board of Trustees through the rulemaking process. The rulemaking hearing is scheduled for April 12th. You may submit comments to the Board of Trustees at rulemaking@mainepers.org through April 27th. If you plan to attend the hearing, please also use that email address to let us know you will attend.

Thank you so much for taking the time to read about these changes. The framework to protect your benefits and budgets from financial market events such as the 2009 recession or other types of market ups and downs was extensively studied over an 18-month period by MainePERS and the PLD Advisory Committee. The actual changes that are included were designed to align the benefits with current industry practices while maintaining a sound benefit for you and your participants.