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April 25, 1996

Claude R. Perrier, Executive Director
Maine State Retirement System
46 State House Station
Augusta, ME 04333-0046

Dear Mr. Perrier:

I am writing in response to your inquiry of last November, posing a number of questions concerning the interpretation of recently enacted amendments to the Maine Constitution dealing with the funding of the Maine State Retirement System and its unfunded liability. Me. Const. art. IX, §§ 18-A, 18-B. I am sorry not to have been able to respond sooner; but, in view of the importance of the questions raised, I wanted to be in possession of the full legislative history of the amendments, the transcripts of the legislative debates of which have only become available in early February, and I wanted to permit members of my staff to discuss our tentative conclusions with you and the Board of Trustees to insure that we were aware of all relevant considerations.

The new constitutional amendments deal generally with three subjects: the funding of the current (or "normal") cost of all retirement and ancillary benefits of the Maine State Retirement System, the creation of new unfunded liabilities for the System, and the liquidation of existing unfunded liabilities. With regard to the first two, Section 18-A provides:

Beginning with the fiscal year starting July 1, 1997, the normal cost of all retirement and ancillary benefits provided to participants under the Maine State Retirement System must be funded annually on an actuarially sound basis. Unfunded liabilities may not be created except those resulting from experience losses. Unfunded liability resulting from experience losses must be retired over a period not exceeding 10 years.

With regard to the third subject, Section 18-B provides:

Each fiscal year beginning with the fiscal year starting July 1, 1997, the Legislature shall appropriate funds that will retire in 31 years or less the unfunded liabilities of the Maine State Retirement System that are attributable to state employees and teachers. The unfunded liabilities referred to in this section are those determined by the Maine State Retirement System's actuaries and certified by the Board of Trustees of the Maine State Retirement System as of June 30, 1996.

You have asked a number of questions related to these subjects. The Opinion of this Department regarding those questions is as follows:

I. Questions Relating to Section 18-A.

A. Ancillary Benefits.

Your first question concerns the interpretation of the words "retirement and ancillary benefits" contained in Section 18-A. Your question is whether these words encompass not only service retirement benefits awarded by the Retirement System, but also disability retirement benefits, death benefits,¹ and group life insurance benefits. For the reasons which follow, it is the Opinion of this Department that the constitutional provision was intended to encompass service retirement benefits, disability retirement benefits, and death benefits, but not benefits that may be available under the Group Life Insurance Program administered by the Retirement System.

The legislative history of the terms in question is silent with regard to their scope. Thus, they may be interpreted only by reference to their plain meaning and the context in which they are employed. Since the amendment in terms refers to "retirement" benefits, it appears clear that benefits referred to in the Retirement System's statutes denominated "retirement" benefits would be covered by the amendment. The retirement statutes contain two types of benefits so denominated,

¹Your question refers to "survivors' benefits," which are denominated "death benefits" by the retirement statutes. 5 M.R.S.A. § 17951 et seq. Also included in this category of benefits are "accidental death benefits" established by 5 M.R.S.A. § 18001 et seq.

both of which are applicable to State employees and teachers.² Those benefits are service retirement benefits, 5 M.R.S.A. § 17851 et seq., and disability retirement benefits, 5 M.R.S.A. § 17921 et seq. These benefits are, therefore, clearly covered by the constitutional amendment.

With regard to death benefits and group life insurance benefits, which cannot be considered "retirement" benefits, the issue becomes whether these benefits are "ancillary" to retirement benefits, within the meaning of the constitutional provision. Death benefits, made available to state employees and teachers by 5 M.R.S.A. § 17951 et seq. ("ordinary death benefits") and § 18001 et seq. ("accidental death benefits"), would appear to fit within this category. These benefits are intended to compensate certain designated beneficiaries for the death of a member of the System prior to the member's service retirement. In the case of ordinary death benefits, the member's beneficiary is entitled to one of three options: the return of the member's contributions; a survivor benefit in a specified amount based upon the type of beneficiary; or, since July 1, 1993, a benefit calculated as if the member had retired on service retirement on the date of his or her death. 5 M.R.S.A. §§ 17953. In the case of accidental death benefits, the beneficiary receives a benefit calculated on the basis of the member's average final compensation. 5 M.R.S.A. § 18003. These benefits are thus clearly "ancillary" to the service retirement benefit, since they are available only to members of the Retirement System and can be a function of either of the amount of the member's contributions or the amount of his or her creditable service and average final compensation.

The situation is less clear, however, with regard to benefits deriving from participation in the Group Life Insurance Program established by 5 M.R.S.A. § 18051 et seq. Under this program, the Board of Trustees is directed to purchase a group life insurance policy or policies under which the designated beneficiaries of persons participating in the program may receive a payment roughly equal to the annual salary of the insured in the event of the insured's death or twice the salary in the event of the insured's accidental death, in addition to which the insured may receive a payment of all or half of the salary in the event of various specified kinds of dismemberments. 5 M.R.S.A. §§ 18056(1). Under current law, state employees and teachers pay no part of the premium for this "basic" coverage. In addition, all participants in the program may purchase additional insurance for themselves in amounts up to three times each person's salary, and may elect to purchase insurance on his or her spouse and/or dependent children. 5 M.R.S.A. § 18056(2) and (3).

²Since neither Section 18-A or Section 18-B applies to the other class of members of the Retirement System--employees of participating local districts (see the response to Question IB, infra)--the chapters of the Retirement Laws relating to the PLDs are not affected. 5 M.R.S.A. § 18201 et seq. (Chapters 425 and 427)

More important for present purposes, however, participation in the Group Life Insurance Program is not a function of membership in the Retirement System. State employees and teacher members may elect not to participate, 5 M.R.S.A. § 18058(2); and, conversely, the program is available to persons who are simply eligible for membership in the Retirement System, whether or not they actually are members. 5 M.R.S.A. §§ 18055. Thus, as indicated above, benefits are generally calculated as a function of the insured's salary, and not as a function of such Retirement System concepts as "creditable service" or "average final compensation." Therefore, group life insurance benefits cannot be considered "ancillary" to retirement benefits.³ The Group Life Insurance Program is simply a different benefit program which the Legislature has chosen to entrust to the Retirement System to administer, but which could be administered by some other State agency or abolished by the Legislature at its discretion.

B. Participating Local Districts.

Your next question is whether the provisions of Section 18-A apply to all participants in the Retirement System, including participating local districts (PLDs) and their employees, or only to the State and its employees and to teachers. The significance of your question is that if the provision applies only to the State and its employees and to teachers, it would serve as a limitation only on the State Legislature (which pays the employer's contribution for both of these classes of participants); but if the provision extends to the participating local districts and their employees, it would exert a limitation on funding of the normal cost of retirement and the creation of unfunded liabilities by those entities as well. In the view of this Department, however, the provision was intended to apply to State employees and teachers only.

The principal reason why this Department reaches this conclusion derives from an examination of the legislative history of Legislative Document 158, the bill which contained both Sections 18-A and 18-B. L.D. 158 (117th Legis. 1995). After holding hearings on the bill, the majority of the Joint Standing Committee on Labor reported to the full Legislature that it "Ought to Pass" in amended form. Comm. Amend. A to L.D. 158, No. S-276 (117th Legis. 1995). A minority of the Committee, however, felt the bill should be enacted in a different form. Comm. Amend. B to L.D. 158, No. S-277 (117th Legis. 1995). The majority report contained the amendments as ultimately adopted; the minority favored the inclusion of a

³Moreover, the fact that the Legislature has directed the Board of Trustees to purchase a life insurance policy or policies does not create an unfunded liability for the assets of the Retirement System. Since the purpose of Section 18-A is to prevent the creation of such liabilities, group life insurance benefits cannot be considered, for this additional reason, to be "ancillary benefits" for purposes of that section.

provision that would allow the Legislature to suspend funding otherwise required by Section 18-A if the Governor certified that a severe economic emergency was present and 7/8 of the membership of each House concurred. The substance of the dispute between the majority and the minority of the Committee, as well as the record of the discussion in the House of Representatives on the only day the bill was debated in either House of the Legislature, reveals that all concerned were operating on the assumption that the objective of Section 18-A was to insure the sound actuarial funding of the normal cost of retirement benefits and the prevention of the creation of new unfunded liabilities by the Legislature. See, e.g., remarks by Rep. Joy ("For years the State has been robbing Peter to pay Paul. They have been withholding funds and not putting them in the Retirement System."); Rep. Winsor ("I am also very aware of the massive amount of unfunded liability that past Legislatures have allowed to grow . . ."); Rep. Tuttle ("I feel that by [voting for the bill] we do the taxpayers of this State a great service . . .") and Rep. Cameron (expressing concern about the welfare of "state employees in the future") (emphasis added) on June 23, 1995.⁴

There is no indication anywhere in the written record of the legislative history of L.D. 158 that the Legislature was considering the funding of normal retirement costs or the creation of unfunded liabilities by the participating local districts. Indeed, your agency advises this Department that employer and employee contributions to the Retirement System and earnings thereon by each PLD are held in each PLD's separate account, and that if that PLD's account is exhausted, the assets of the System attributable to the State and teacher plan(s) and to other PLDs are not available to make up any shortfall. Thus, the concerns of the Legislature reflected in the passage of Section 18-A are not affected by any actions of the PLDs. Consequently, this Department concludes that Section 18-A (as well as Section 18-B which expressly applies only to the State) was not intended to apply to them.

C. Funding of Increased Benefits.

You next ask whether Section 18-A means that, if the Legislature were to increase any benefits for the members of the Retirement System in the future, it must simultaneously fund such increases. In order to answer this question, it is necessary to distinguish between two kinds of possible legislative action: action which increases benefits based on creditable service already accrued, and action which increases benefits based on future creditable service.

With regard to the first type of possible legislative action, the second sentence of Section 18-A provides simply that: "Unfunded liabilities may not be created."

⁴At the time of the preparation of this Opinion, the Legislative Record for the House of Representatives for this date had not been paginated.

The enactment by the Legislature of a statute increasing a benefit based on already accrued creditable service without any funding would be a clear case of the creation of an unfunded liability for the Retirement System. The System would be liable to pay the increased benefit at some time in the future, but would not be provided with the funds with which to do so. Thus legislative action of this kind is clearly prohibited.

If, on the other hand, the Legislature were to seek to increase benefits based on future creditable service, such action would also be governed by the first sentence of Section 18-A, which provides, in pertinent part, that "the normal cost of all retirement and ancillary benefits . . . must be funded annually on an actuarially sound basis." The obvious thrust of this provision is that each year the Legislature must determine what funding level, on an annual basis, is required to fund the cost of all existing retirement and ancillary benefits, and that, therefore, if it chooses to increase any benefits prospectively, those increased benefits must be included as part of "all retirement and ancillary benefits" and be adequately funded. In short, therefore, if the Legislature wishes to increase benefits based on future creditable service, the constitutional amendment requires that the cost of such benefits be included within the "normal cost" of existing benefits and funded on an actuarially sound basis.

D. Effective Date of Prohibition Against the Creation of Unfunded Liabilities.

Your next question concerns the effective date of the second sentence in Section 18-A, which provides: "Unfunded liabilities may not be created except those resulting from experience losses." Your question is whether this sentence does not become effective until July 1, 1997, the date contained in the first sentence of Section 18-A which requires the annual funding of all retirement benefits on an actuarially sound basis, or whether it became effective immediately upon the effectiveness of the constitutional amendments themselves, which occurred on November 27, 1995, the date of their proclamation by the Governor. In the view of this Department, the sentence in question became effective upon the Governor's proclamation.

The concern raised by your question is that, if the second sentence were not effective until July 1, 1997, the Legislature would be free to create unfunded liabilities until that time. Such a reading would, however, appear to be inconsistent with the overall intent of the amendment, which is to prevent the creation of new unfunded liabilities and to provide for the orderly retirement of existing unfunded liabilities. That this is the case may be seen not only by the text of the sentence at issue, but also by the provision of Section 18-B that the amount of these unfunded liabilities be fixed by the Retirement System's actuaries effective June 30, 1996. If the Legislature were able to create additional unfunded liabilities until July 1, 1997, the amount of the total unfunded liability related to State employees and teachers

established by the System's actuaries for retirement over 31 years would be inaccurate. Consequently, the prohibition against the creation of new unfunded liabilities must be deemed to have been effective upon the entry into force of both of the constitutional amendments.

E. Manner of Creation of Unfunded Liabilities.

Your fifth inquiry contains a series of questions concerning the manner by which unfunded liabilities may be created, and the consequences of the creation of such unfunded liability. Generally, your questions are whether unfunded liabilities may be created, not only by enhancing benefits, but by inadequate funding of existing benefits; whether the unconstitutional creation of an unfunded liability may result from action not only by the Legislature but by a State agency, a school administrative unit, or a participating local district;⁵ and whether the Board of Trustees is required, by its fiduciary obligations, to take immediate action against any entity creating an unfunded liability to secure adequate funding. Our answers to these questions are as follows:

Section 18-A clearly contemplates that unfunded liabilities may be created not only by the enactment of increased benefits, but by the underfunding of existing benefits. The section provides that after July 1, 1997, the "normal cost of all retirement and ancillary benefits . . . must be funded annually on an actuarially sound basis." The concept of "normal cost" includes an actuarial determination of the amount required to fund benefits as they are earned or accrued. There is no room in this concept for any delay in the funding of such benefits, even on a temporary basis. Thus, the failure of the Legislature to provide adequate funding on an annual basis for benefits earned or accrued must be considered a creation of an unconstitutional unfunded liability.

As indicated in our answer to your second question above, Section 18-A relates to the creation of unfunded liabilities on behalf of state employee and teacher members of the Retirement System. Thus, the prohibition against the creation of unfunded liabilities necessarily extends to any governmental body in a position to create such a liability. This would include not only the Legislature, but state agencies and school administrative units. Therefore, if any of these entities either create new benefits or do not fund existing benefits on an actuarially sound basis, those actions would be unconstitutional.

Article IX, Section 18 of the Maine Constitution provides that the assets of the

⁵As indicated in Part IB of this Opinion, supra, Section 18-A does not apply to the PLDs, so actions of the PLDs cannot violate the section. In responding to this question, therefore, this Opinion will make no further reference to the PLDs.

Retirement System shall be held "as in trust" by the Board of Trustees. This provision thus establishes that the Board has a fiduciary obligation to the members of the Retirement System with regard to the management of funds held in trust by the Retirement System. Such an obligation extends to the assertion of any legitimate claims which the fund may have. Section 18-A, by prohibiting the creation of unfunded liabilities, creates the possibility of a new class of claims to be asserted on behalf of the System's funds. Should such claims in fact arise, it would therefore be the fiduciary obligation of the Board to pursue them. Thus, if the Legislature were to create an unfunded liability, the Board of Trustees would have a fiduciary obligation to respond to such action, such as by refusing to implement the benefit in question until adequate funding was provided.

F. Effective Date of Provision Relating to Experience Losses.

Your final question relating to Section 18-A is whether the third sentence of the section, providing that unfunded liabilities resulting from experience losses must be retired over a period not to exceed 10 years, was effective immediately upon the proclamation of the amendment by the Governor, or is not effective until July 1, 1997. For the reasons set forth in our answer to your fourth question above, it is the Opinion of this Department that this provision was effective on November 27, 1995.

II. Questions Relating to Section 18-B.

A. Covered Employees.

Your first question with regard to the interpretation of Section 18-B concerns the range of coverage of that section. As quoted above, the section concerns the retirement of the existing unfunded liabilities "of the Maine State Retirement System that are attributable to State employees and teachers." In the Retirement System statutes, the terms "State employees" and "teachers" are defined. 5 M.R.S.A. § 17001(40) ("state employee" defined to exclude judges, legislators, and certain members of the State Police"), (42) ("teacher"). The question you present is whether, in enacting the constitutional provision, the Legislature meant to incorporate by reference these definitions, or whether it meant to use them in a broader sense, so as to encompass persons not included in those definitions, such as governors, legislators and judges.

In the Opinion of this Department, in enacting this constitutional provision, the Legislature intended that it apply to all persons eligible to receive retirement and ancillary benefits from the Retirement System; other than employees of participating local districts. As indicated in our answer to question IA, supra, the legislative history of the two constitutional amendments is replete with a general concern on behalf of the Legislature that the unfunded liability of the Retirement System related to State employees and teachers be retired over a fixed period of time. For example, the Statement of Fact to the Committee Amendment which

eventually became the enacted constitutional amendments states that "funds must be appropriated each year to pay off the current unfunded liability of the Retirement System over 31 years or less." Comm. Amend. A to L.D. 158, No. S-276, Statement of Fact (117th Legis. 1995). Similar general statements were made by proponents of the amendments on the floor of the House of Representatives, in which concern was expressed about the actions of past Legislatures in both creating unfunded liabilities and postponing the payment of them. Remarks of Reps. Joy, Winsor, Chase, Tuttle and Hatch on June 23, 1995.⁶ In none of these statements is there any indication that the Legislature, in using the terms "state employees and teachers" in the text of Section 18-B, was using these terms in the technical sense in which they appear in Section 17001 of the retirement statutes. Rather, the intention was to ensure that all unfunded liabilities of the Retirement System attributable to members whose employer contribution is made by the State government should be extinguished in 31 years. Thus, the provision should be read to include participants in the Governor's Retirement Fund, 2 M.R.S.A. § 1-A; the Maine Legislative Retirement System, 3 M.R.S.A. § 701 et seq.; and the Maine Judicial Retirement System, 4 M.R.S.A. § 1201 et seq.⁷

B. Manner of Fixing Amount of Unfunded Liability.

Your final question concerns the fixing of the amount of the unfunded liability that will be retired over 31 years. You ask whether the amendment "in effect constitutionalizes the current amortization methodology, fixes the resulting amortization schedule as of June 30, 1996, and requires that the schedule remain unchanged for the succeeding 31 years."

As quoted above, the text of Section 18-B defines the unfunded liabilities at issue as those "determined by the Maine State Retirement System's actuaries and certified by the Board of Trustees of the Maine State Retirement System as of June 30, 1996." The amendment then provides that this amount shall be retired over 31 years. The likely reason why the Legislature fixed on 31 years as the amount of time required to retire the unfunded liability related to State employees and teachers is that, in 1993, it statutorily established a 35 year schedule which will have 31 years remaining on June 30, 1997. P.L. 1993, ch. 410, § L-51. Your first question, therefore, is whether the amendment constitutionalizes the current amortization methodology.

⁶At the time of the preparation of this Opinion, the Legislative Record for the House of Representatives for this date had not been paginated.

⁷Consistent with this view, it is also our opinion that the term "participants" in Section 18-A encompasses not only State employees and teachers, but also to governors, legislators and judges.

There is no indication in the legislative history of what had the Legislature had in mind in enacting this provision. Nor, to the knowledge of this Department, do the existing statutes direct that any particular amortization methodology be employed. Under these circumstances, therefore, this Department is reluctant to conclude that the constitutional amendment directs that any particular methodology be employed, other than that the methodology employed must produce an actuarially sound result generally.

With regard to your remaining two questions, the constitutional language is also unclear. Section 18-B requires only that "Each fiscal year . . . the Legislature shall appropriate funds that will retire in 31 years or less the unfunded liabilities of [the System] that are attributable to state employees and teachers." There is no provision, therefore, that the Legislature adhere to any particular schedule in complying with this provision, other than that the Legislature must make some appropriation for each fiscal year. Thus, the Legislature remains free to vary the pace of its payments to retire the unfunded liability, so long as the liability is retired in 31 years or less after July 1, 1997. This is not to say that it would not be sound practice for the Legislature to adhere to a fixed payment schedule; it is only to say that such a schedule is not constitutionally required.

I hope the foregoing answers your questions. Please feel free to reinquire if further clarification is necessary.

Sincerely,

A handwritten signature in black ink, appearing to read "Andrew Ketterer", written in a cursive style.

ANDREW KETTERER
Attorney General

AK:sw

cc: Governor Angus S. King, Jr.
President Jeffrey H. Butland
Speaker Dan A. Gwadosky
Senator Charles M. Begley
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Co-chairs, Joint Standing Committee on Labor