Department of Legislative Services
Maryland General Assembly
2010 Session

FISCAL AND POLICY NOTE

House Bill 1113 (Delegate Stocksdale, *et al.*)
Appropriations

State Retirement and Pension System - Retirement Allowance Adjustments

This emergency bill specifies that, if the calculation of the cost-of-living adjustment (COLA) for retirees and beneficiaries of designated plans of the State Retirement and Pension System (SRPS) results in a negative adjustment in a given year, there is no COLA for that year.

Fiscal Summary

State Effect: State pension liabilities increase by approximately $88.2 million due to holding retirees and beneficiaries harmless from a negative COLA calculation for FY 2011. Amortizing those liabilities over 25 years results in State pension contributions increasing by $5.9 million in FY 2012 and increasing annually according to actuarial assumptions. Costs for teachers are paid entirely by general funds, while costs for State employees are assumed to be allocated 60% general funds, 20% special funds, and 20% federal funds. COLA calculations are not anticipated to be negative again within the next five years. No effect on revenues.

($ in millions)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
Revenues	$0	$0	$0	$0	$0
GF Expenditure	0	4.95	5.12	5.30	5.49
SF Expenditure	0	.47	.49	.50	.52
FF Expenditure	0	.47	.49	.50	.52
Net Effect	$.00	($5.89)	($6.10)	($6.31)	($6.53)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: Local pension liabilities for participating governmental units (PGUs) increase by approximately $5.5 million. Amortizing those liabilities over 25 years results in PGU employer contributions increasing by $366,000 in FY 2012 and increasing annually according to actuarial assumptions. Those costs are shared among approximately 120 PGUs.

Small Business Effect: None.

Analysis

Bill Summary: The bill applies to COLA calculations for former members, retirees, and surviving beneficiaries of the following SRPS plans:

- Employees' and Teachers' Pension Systems (EPS/TPS) who receive either a simple or compounded COLA capped at 3%;

- Teachers' or Employees' Retirement System (TRS/ERS) who receive a compounded COLA capped at 5%; and

- Law Enforcement Officers' Pension System (LEOPS).

Current Law: Each year, retirement allowances paid to SRPS retirees and beneficiaries are adjusted for inflation. All COLA calculations are based on average annual changes to the Consumer Price Index (CPI) for all urban consumers (CPI-U), but the amount and type of COLA varies by system. In general, the various statutory COLA provisions do not prohibit a negative adjustment. COLAs are applied to retiree and beneficiary allowances effective July 1 of each fiscal year based on the average CPI-U as of December 31 of the previous fiscal year (*e.g.*, the fiscal 2011 retiree COLAs are calculated based on the CPI-U in calendar 2009).

EPS/TPS and LEOPS retirees and beneficiaries receive annual compounded COLAs, subject to a 3% cap. However, EPS/TPS retirees and beneficiaries of the noncontributory (pre-1998) EPS receive simple (noncompounding) COLAs, also subject to a 3% annual cap. Only eight PGUs, most notably Prince George's County government, participate in noncontributory EPS.

State Police Retirement System (SPRS), Correctional Officers' Retirement System (CORS), and ERS/TRS retirees and beneficiaries subject to Selection A (*i.e.*, contributed 7% of earnable compensation while active) receive unlimited, compounded COLAs.

ERS/TRS retirees and beneficiaries subject to Selection B (*i.e.*, contributed 5% of earnable compensation while active) receive annual compounded COLAs, subject to a 5% cap. ERS/TRS retirees and beneficiaries subject to Selection C (a bifurcated benefit) receive a two-part COLA. For service credit earned under ERS/TRS, the COLA is unlimited. For service credit earned after choosing Selection C, the COLA is subject to a 3% cap.

Retirees and beneficiaries of the Legislative Pension Plan and the Judges' Retirement System do not receive automatic COLAs, and they are not affected by this bill. Their benefits are linked to the salaries of active legislators and judges, respectively. Therefore, their benefits increase whenever salaries for active members are raised.

Background: The CPI-U declined by 0.356% over the previous year as of December 31, 2009. Specifically, the average CPI-U index was 214.5 for 2009, compared with 215.3 for 2008. This is the first decline in CPI-U on an annual basis since 1954. **Exhibit 1** shows the annual percentage changes in the CPI-U since 2000. As the exhibit shows, the CPI-U has exceeded 3% in 4 of the last 10 years, but has not exceeded 5% in any of those years.

Exhibit 1
Annual Percentage Changes in CPI-U
Calendar 2000-2009

Year	% Annual Change
2000	3.4
2001	2.8
2002	1.6
2003	2.3
2004	2.7
2005	3.4
2006	3.2
2007	2.8
2008	3.8
2009	-0.4

Source: U.S. Bureau of Labor Statistics

The statutory language governing the various COLA calculations generally does not preclude the application of a negative COLA, which would result in a reduction to retirees' and beneficiaries' annual allowances. However, retirees of SPRS, CORS, and ERS/TRS who are subject to the unlimited COLAs cannot receive an allowance in a given year that is less than their initial allowance. Therefore, retirees of those systems who are in their first year of retirement are protected against a negative COLA because the initial allowance they are receiving this year cannot be reduced.

Exhibit 2 shows the number of retirees and beneficiaries in each of the State's major employee pension and retirement plans and their average monthly benefit in fiscal 2009.

Exhibit 2
SRPS Retirees and Beneficiaries
June 30, 2009

Plan	Retirees and Beneficiaries	Average Monthly Benefit
TRS	30,598	$2,600
TPS	25,158	$1,457
ERS (includes CORS)	23,778	$1,530
EPS	32,832	$905
SPRS	2,226	$3,525
LEOPS	1,067	$2,551

Source: State Retirement and Pension System

State Fiscal Effect: The Department of Legislative Services (DLS) assumes that SRPS would, in the absence of this bill, reduce retirees' and beneficiaries' fiscal 2011 retirement allowances by 0.356% from their fiscal 2010 levels due to a negative COLA calculation for all affected SRPS plans. Based on that assumption, the General Assembly's actuary estimates that freezing fiscal 2010 allowances at their current levels for one year results in an $88.2 million increase in State pension liabilities. Amortizing that liability over 25 years results in a first-year increase in State pension contributions of $5.9 million in fiscal 2012. Those contributions increase annually according to actuarial assumptions.

Based on current projections, DLS does not expect that the bill applies again within the five-year period covered by this fiscal and policy note.

DLS notes that, as drafted, the bill does not apply to retirees of three systems with uncapped COLAs: SPRS, CORS, and TRS/ERS Selection A retirees; it also does not apply to TRS/ERS Selection C retirees who receive a bifurcated COLA. DLS assumes that the intent of the bill is to apply to all SRPS retirees. The fiscal analysis reflects that assumption.

Local Fiscal Effect: Local pension liabilities increase by approximately $5.5 million; amortizing those liabilities over 25 years yields a first-year cost of $366,000 in fiscal 2012. That cost is presumed to grow annually according to actuarial assumptions and is shared by approximately 120 PGUs.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Mercer Human Resources Consulting, Maryland State Retirement Agency, Department of Legislative Services

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Analysis by: Michael C. Rubenstein

Direct Inquiries to:
(410) 946-5510
(301) 970-5510