

Department of Legislative Services
Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE

House Bill 808
Appropriations

(Delegate Griffith)(Chair, Joint Committee on Pensions)

Budget and Taxation

State Retirement and Pension Systems - Cost-of-Living Adjustments - Clarification

This bill makes technical and clarifying changes to the statutory provisions addressing annual cost-of-living adjustments (COLAs) for retirees of the State Retirement and Pension System (SRPS).

The bill takes effect July 1, 2012.

Fiscal Summary

State Effect: None. The bill is technical and clarifying in nature.

Local Effect: None.

Small Business Effect: None.

Analysis

Bill Summary: The bill makes the following clarifications with respect to COLA calculations:

- each type of COLA calculation in State law does not apply to benefits paid in a single payment, the return of accumulated contributions, or benefits attributable to additional contributions;
- COLAs are to be calculated using a specific rate rather than a fraction;
- COLAs in a zero-adjustment fiscal year do not apply to a retiree's or former member's first COLA adjustment; and

- a retiree may not receive a negative COLA that would result in a benefit that is less than the retiree's initial allowance.

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, but the amount and type of COLA varies by system. In general, the various statutory COLA provisions do not prohibit a negative adjustment. However, Chapters 56 and 57 of 2010 specified that, if the calculation of the 2010 COLA for retirees and beneficiaries of designated SRPS systems resulted in a negative adjustment, retirement allowances were not to be adjusted for fiscal 2011. They also required, if fiscal 2011 allowances were not adjusted because of a negative COLA calculation, that fiscal 2012 allowances be reduced by the difference between the fiscal 2010 allowances and the allowances that would have been paid in fiscal 2011 if they had been adjusted. They also included a related study and reporting requirement for the SRPS Board of Trustees. Based on the report submitted by the board, Chapter 599 of 2011 made those changes permanent and also required the board to submit a report with recommended technical and clarifying changes to the COLA provisions; this bill implements the board's recommendations.

COLAs are applied to retiree and beneficiary allowances effective July 1 of each fiscal year based on the average CPI as of the second prior December 31. Retirees and beneficiaries of the Legislative Pension Plan (LPP) and the Judges' Retirement System (JRS) do not receive automatic COLAs. Their benefits are linked to the salaries of active legislators and judges, respectively. Therefore, their benefits increase whenever salaries for active members are raised.

Following the enactment of Chapter 397 of 2011, COLA benefits for SRPS retirees are calculated separately for service credit earned prior to July 1, 2011, and service credit earned on or after that date.

COLAs for Pre-2011 Service Credit

State Employees' and Teachers' Pension Systems (EPS/TPS) and the Law Enforcement Officers' Pension System 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 six participating governmental units, most notably Prince George's County government, participate in noncontributory EPS.

Retirees and beneficiaries of the State Police Retirement System (SPRS), Correctional Officers' Retirement System, and Employees' or Teachers' Retirement Systems

(ERS/TRS) 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, COLA is unlimited. For service credit earned after choosing Selection C, COLA is subject to a 3% cap.

Chapter 122 of 1999 increased the retirement allowances of SPRS retirees and beneficiaries of retirees who retired before June 30, 1999, by providing annual lump-sum payments, as follows:

- \$1,200 for retirees who had been retired not more than 5 years;
- \$1,500 for retirees who had been retired more than 5 years but less than 10 years;
- \$1,800 for retirees who had been retired more than 10 years but less than 15 years; and
- \$2,100 for retirees who had been retired more than 15 years.

Retirees and beneficiaries receive an annual unlimited COLA on the annual lump-sum payment in addition to their existing benefit and COLA.

COLAs for Post-2011 Service Credit

Chapter 397 linked COLA benefits for service credit earned on or after July 1, 2011, to the investment performance of the SRPS trust fund. The changes apply to all SRPS plans, except ERS/TRS, LPP, and JRS. COLA adjustments for a given year are equal to CPI up to 2.5% for any year in which the pension trust fund achieves its target rate of return, currently set at 7.75%. In years when the investment return falls short of the target, the COLA adjustment is equal to CPI up to 1.0%.

Background: Automatic annual COLAs for SRPS members based on CPI date back to 1971 with the enactment of Chapter 424. CPI had never been negative since that time until December 2009. This was the first decline in CPI on an annual basis since 1954. **Exhibit 1** shows the annual percentage changes in CPI since 2000. As the exhibit shows, CPI has exceeded 3% in 5 of the last 12 years, but it has not exceeded 5% in any of those years. It exceeded 2.5% in 8 of the last 12 years, and 1.0% in all but 1 year.

Exhibit 1
Annual Percentage Changes in CPI for All Urban Consumers
Calendar 2000-2011

<u>Year</u>	<u>% Annual Change</u>
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%
2010	1.6%
2011	3.2%

Source: U.S. Bureau of Labor Statistics; Maryland State Retirement Agency

Additional Information

Prior Introductions: None.

Cross File: SB 879 (Senator Jones-Rodwell)(Chair, Joint Committee on Pensions) - Budget and Taxation.

Information Source(s): Maryland State Retirement Agency, Department of Legislative Services

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