SB 1

Department of Fiscal Services

Maryland General Assembly

FISCAL NOTE
Revised

Senate Bill 1 (Senator Miller, et al.)
Budget and Taxation | Referred to Appropriations

Workforce Reduction Act

This enrolled pension bill establishes an early retirement incentive plan for State employee members of the employees' retirement (ERS) and pension systems (EPS). Members are eligible to participate if they are currently eligible to retire or have at least: (1) 25 years of service and are age 50 or over; or (2) 20 years of service and whose positions are abolished before June 30, 1997. Unused sick leave is not counted as creditable service for eligibility purposes. Members who are not laid off must apply between July 1 and August 31, 1996. Participants receive one month of additional service credit for each year of creditable service. Up to 18% (three years) of the reduction for early retirement is eliminated. The increase in the State's actuarial liability resulting from this incentive plan will be amortized over five years (beginning in fiscal 1998). The bill also provides a 100% subsidy of health insurance, for one year, for laid-off employees.

The Department of Budget and Fiscal Planning must eliminate at least 60% of the vacated positions by November 1, 1996, with exceptions. The bill provides for the delayed early retirement of those eligible members who work in units of State government which have more than 5% of their workforce eligible to participate in the early retirement incentive plan. No more than 2% of employees retiring under the bill may be reemployed in a contractual or temporary position in any branch of State government. The earnings limitation for participating employees is based on the retirement benefit received including that portion of the benefit resulting from the incentives received for early retirement.

The bill does not apply to employees of: (1) the Judicial branch of government; (2) an institution of higher education (defined); or (3) off-budget agencies. Reduced general and special fund appropriations resulting from the bill will be transferred by budget amendment to the general fund and appropriate special funds, respectively.

Fiscal Summary

State Effect: Significant personnel expenditure decrease beginning in FY 1997 and significant retirement expenditure increase beginning in FY 1998, both as discussed below. One-time special fund administrative expenditure increase of $192,000 in FY 1996. Revenues would not be affected.

($ in millions)	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001
GF Expenditures	($13.5)	($30.0)	($30.0)	($30.0)	($30.0)
SF Expenditures	(4.5)	(10.0)	(10.0)	(10.0)	(10.0)
FF Expenditures	(4.5)	(10.0)	(10.0)	(10.0)	(10.0)
Net Effect	($22.5)	($50.0)	($50.0)	($50.0)	($50.0)

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

Local Effect: None.

Fiscal Analysis

State Expenditures: The Retirement Agency has identified 7,565 employees who are eligible for the early retirement incentive plan, of which it is estimated 2,525 will participate. There are four significant areas of fiscal impact: (1) salary savings; (2) retirement costs; (3) retiree health care costs; and (4) administrative costs.

<u>Salary Savings</u>

The bill provides that 60% of the retiring members positions be abolished from the State budget. Salary savings would result from the elimination of positions included in the budget. The salary savings estimates are based on the following assumptions: (1) the average salary of eligible members of the retirement system is $37,500 and the average salary of eligible members of the pension system is $34,600; (2) fringe benefits at the rate of 18% of salary; (3) an annual health insurance subsidy of $3,926; (4) retiring employees have 45 days of unused annual leave, or $7,314; and (5) on average, all abolished positions will be vacant for six months in fiscal 1997. Based on these assumptions, each abolished position would result in a savings of $15,778 in fiscal 1997 and $46,184 on an annualized basis.

Based on the estimated participation of 2,525 employees, 1,515 positions would be eliminated (2,525 x 60%) resulting in a fiscal 1997 savings of $23.9 million (all funds) and $70.0 million in fiscal 1998 and beyond.

Retirement Costs

Retirement costs are estimated in three areas: (1) cost of one additional month of service credit for each year of service; (2) cost of eliminating up to three years of the actuarial reduction; and (3) cost of early retirement for laid-off employees.

The State's actuary estimates that the retirement incentive provided in the bill (one month of additional service credit for each year of service) would increase the actuarial liabilities of the systems at the rate of $25.0 million for each 1,000 members receiving the benefit. The bill requires that the actuarial liabilities created by the incentives be amortized and funded over five years. Thus, first year annual retirement contributions would increase by $5.3 million per 1,000 members receiving the incentive. These costs would increase by 5% each year until the liability is fully funded.

The State's actuary has estimated that approximately 900 employees would benefit from the elimination of up to 18% (three years) of the actuarial reduction for early retirement. The actuary has estimated that such benefits would increase the actuarial liabilities of the system by $25 million. The State's actuary has estimated that actuarial liabilities could increase by approximately $80,000 per laid-off employee. While the number of such layoffs is unknown, for purposes of this estimate, it is assumed that 100 laid-off employees would be eligible for early retirement resulting in an increase of $8.0 million in actuarial liabilities.

Thus, the actuarial liabilities of the systems could increase by $97 million. Funding such costs over five years would require a first year contribution of approximately $20 million in fiscal 1998. Such expenditures would increase by 5% each year until the liability is fully funded.

Health Insurance Costs

The bill provides a 100% subsidy of health insurance coverage, for one year, for employees whose positions are abolished by the Governor between January 1, 1996 and June 30, 1997. Assuming that 210 laid-off employees would be eligible for one year of health insurance benefits, health insurance expenditures could increase by $1,030,470 (210 x $4,907) in fiscal 1997.

Administrative Costs

The Retirement Agency has indicated that special fund expenditures could increase by $192,000 in fiscal 1996 and $367,000 in fiscal 1997. Such costs would be required to provide information to employees eligible for the incentive program and to process retirement requests.

Summary: Based upon the fiscal estimates presented above, fiscal 1997 expenditures could decrease by $22,534,000. Out-year expenditures could decrease by approximately $50 million annually beginning in fiscal 1998. It is estimated that such reductions would be split 60%, 20%, and 20% between general, special, and federal funds respectively.

Additional Comments: The Department of Fiscal Services advises that approximately 1,500 members of the employees' retirement and pension systems will retire in fiscal 1997 under current law. Fiscal Services further advises that the estimated salary savings are dependent upon the abolishment of positions with average salaries from $34,600 to $37,500. If the positions abolished by the Governor have salaries below this level, realized salary savings could be greatly reduced. Further, this estimate does not include any adjustment to reflect promotions or salary increases for other employees that result from employees retiring as a result of this bill. Moreover, long-term salary savings are dependent upon a permanent reduction in the size of the State workforce. If additional positions are created in the future as a result of this downsizing, salary savings would be significantly reduced.

Information Source(s): Milliman and Robertson, Inc.; State Retirement Agency; Department of Fiscal Services

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