Department of Fiscal Services

Maryland General Assembly

FISCAL NOTE

House Bill 1250 (Delegate Rosenberg)
Appropriations

Workforce Reduction Act - Purchase of Service Credit

This pension bill alters the method by which the cost of purchasing service credits under the Workforce Reduction Act of 1996 (SB 1, Chapter 353) is calculated, both for members who chose to purchase such credits and those who did not. The bill provides for partial refunds to individuals who purchased service credits in order to retire under SB 1. Also, the bill allows those members who received estimates for the cost of purchasing service credits and who opted not to purchase service credits to do so now, and receive the same early retirement benefits that were available under SB 1 of 1996. The bill is effective June 1, 1997.

Fiscal Summary

State Effect: Personnel expenditures would decrease by $2.6 million in FY 1998; future years reflect a decrease in personnel expenditures offset by an increase in retirement expenditures. One-time special fund administrative expenditure increase of $34,000 in FY 1998. Revenues would not be affected.

($ in millions)	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002
GF/SF/FF Rev.	$0	$0	$0	$0	$0
GF/SF/FF Expend.	($2.6)	($2.8)	($2.7)	($2.6)	($2.5)
Net Effect	$2.6	$2.8	$2.7	$2.6	$2.5

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

Local Effect: None.

Small Business Effect: None. This bill would not directly affect small businesses.

Fiscal Analysis

Bill Summary: The bill provides for partial refunds to individuals who purchased service credits in order to retire under SB 1 of 1996, with the retiree being refunded for the amount the retiree paid equal to the annuity reserve and pension reserve required to fund the increase in allowance resulting from any additional service credit or reduction of early retirement penalty provided for under SB 1.

Also, the bill allows those members who last year received estimates for the cost of purchasing service credits and who opted not to purchase service credits last year to do so now, and receive the same early retirement benefits that were available under SB 1. The cost of these service credits would equal the annuity reserve and pension reserve required to fund the additional allowance attributable to the service credit purchased. The price of the service credit cannot include the annuity reserve or pension reserve attributable to an increase in allowance resulting from any additional service credit or reduction of an early retirement penalty provided under SB 1 of 1996.

Under the bill, a member who purchases such service credit at the new price and becomes eligible for early retirement as established by SB 1 of 1996 may submit an application for early retirement between July 1 and September 1, 1997. Applicants would retire on October 1, 1997.

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 1999).

The Department of Budget and Management must eliminate at least 60% of the vacated positions by November 1, 1997, 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.

State Expenditures: Employees who sought to purchase service credit in order to retire under SB 1 of 1996 were given estimates that included: (1) the full actuarial costs of the additional months of service credit provided under SB 1; (2) the full costs of the reduction in early retirement penalties provided under SB 1; and (3) the additional years of benefits that would be paid and employer contributions that would be foregone as a result of the member retiring sooner than they would have absent SB 1. Under this bill, members who purchased service credits would receive refunds for the costs associated with the second and third items; the revised purchase price would include only the costs associated with the additional service credits provided by SB 1. Similarly, those people who had received estimates for purchases of service credit would receive new estimates based solely on the costs associated with the additional service credits.

Twenty-two former State members of the employees' retirement and pension systems purchased service credit in order to elect early retirement under SB 1. These payments ranged between $270 and $102,570. The average payment was $19,642. The State's actuary estimates that the average purchase of service credit under the new cost formula would be approximately $10,200 per person for those who purchased such credits. Thus, the actuary estimates that those who purchased credits are likely to receive refunds of approximately $9,450 on average, for a total cost to the State of $207,900.

Approximately 600 members received estimates of the cost of purchasing service credit. The actuary estimates that, on average, the new estimates will be approximately $14,200 lower than the previous estimates. It is estimated that approximately 180 (or 30%) of those who receive a new estimate will elect early retirement. This will result in elimination of 108 full-time equivalent (FTE) positions. There are three significant areas of fiscal impact: (1) salary savings; (2) actuarial costs; and (3) administrative costs.

Salary Savings

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 Employees' Retirement System (ERS) is $36,629 and the average salary of eligible members of the Employees' Pension System (EPS) is $29,691; (2) fringe benefits at the rate of 18% of salary; (3) retiring employees have 50 days of unused annual leave, or approximately $6,800 per person; and (4) on average, all abolished positions will be vacant for 3.5 months in fiscal 1998.

For those 180 members electing early retirement, it is estimated that the fiscal 1998 net salary savings (less time worked in fiscal 1998 and leave payout multiplied by 60%) would equal $2.6 million. Fiscal 1999 and out-year salary savings are estimated to be $4.6 million, or 60% of the salaries associated with the vacated positions.

Actuarial Costs

Actuarial costs are estimated in three areas: (1) cost of refunds to former members who already purchased service credits; (2) cost of the reduction in the price of such credits for those who choose to purchase such credits now; and (3) the costs of the early retirement incentives for the 180 new retirees. It is estimated that these changes would increase the actuarial liabilities of the systems by a total of $8.6 million. These additional liabilities must be funded over five years beginning in fiscal 1999. The 1999 payment would $621,000. These costs would increase by 5% each year until the liability is fully funded, as shown below.

Actuarial Costs

	Refund Costs	New Participant Costs	Early Retirement Costs	Total
1999	$47,000	$574,000	$1.3 million	$1.9 million
2000	$49,000	$603,000	$1.3 million	$2.0 million
2001	$52,000	$633,000	$1.4 million	$2.1 million
2002	$54,000	$664,000	$1.5 million	$2.2 million
2003	$57,000	$697,000	$1.5 million	$2.3 million

Administrative Costs

It is estimated that administrative expenditures by the State Retirement Agency to implement this proposal would total $34,000. Such costs would be required to provide information to employees eligible for the incentive program and to process retirement requests. Certain computer charges for programming incurred for SB 1 will not be incurred again.

Summary: Based upon the fiscal estimates presented above, fiscal 1998 expenditures could decrease by $2.6 million. Out-year expenditures could decrease by approximately $2.8 million beginning in fiscal 1999, as illustrated below.

Effect on Expenditures ($ in Millions)
(numbers may not sum due to rounding)

	1998	1999	2000	2001	2002
Salary Expenditures	($2.6)	($4.6)	($4.6)	($4.6)	($4.6)
Actuarial Costs	0.0	1.9	2.0	2.1	2.2
Administrative Costs	(0.0)	0.0	0.0	0.0	0.0
Net Effect	$2.6	$2.8	$2.7	$2.6	$2.5

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 its 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): State Retirement Agency, Milliman & Robertson, Inc., Department of Fiscal Services

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