Department of Legislative Services

Maryland General Assembly
2000 Session

FISCAL NOTE
Revised

House Bill 421 (Delegate Proctor)
(Chairman, Joint Committee on Pensions)

Appropriations

Employees' and Teachers' Pension Systems - Contributory Pension Benefit

This pension bill creates break-in-service provisions for the new contributory Employees' Pension System (EPS) and Teachers' Pension System (TPS) and changes the treatment of former vested members who have returned to membership after June 30, 1998.

The bill takes effect July 1, 2000.

Fiscal Summary

State Effect: Increase in pension liabilities of $16.7 million, resulting in increased employer pension contributions of $1.1 million in FY 2002, increasing in future years based on actuarial assumptions. Revenues would not be affected.

(in dollars)	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
All Revenues	$0	$0	$0	$0	$0
GF Expenditures	0	925,700	972,000	1,020,500	1,071,700
SF Expenditures	0	103,700	108,900	114,300	120,000
FF Expenditures	0	103,700	108,900	114,300	120,000
Net Effect	$0	($1,133,100)	($1,189,700)	($1,249,100)	($1,311,700)

Note: ( ) = decrease; GF = general funds; FF = federal funds; SF = special funds; - =indeterminate effect
Numbers may not total due to rounding.

Local Effect: Contributions by local government units that participate in the State Retirement and Pension System (SRPS) and that elected the enhancement could increase in aggregate by $130,000 per year, based on an increase in liabilities of $2.0 million.

Small Business Effect: None.

Analysis

Bill Summary: This bill creates provisions for the contributory Employees' Pension System (EPS) or the Teachers' Pension System (TPS) regarding breaks in service and former vested membership.

- Membership in the contributory EPS and TPS continue for *four* years after separation from employment unless the member withdraws his or her accumulated contributions, becomes a retiree, or dies.

- On the return of accumulated contributions of former members of the contributory EPS or TPS, the former members are not entitled to further benefits on account of membership in the systems. These former contributory EPS or TPS members, however, can redeposit withdrawn member contributions (plus interest) and repurchase previously forfeited service.

- Members of the contributory EPS or TPS receive eligibility service credit for prior service if: (1) the member was entitled to a vested EPS or TPS benefit at the time of separation from the first stretch of employment; (2) the member has either not withdrawn his or her contributions or has redeposited those contributions; and (3) the member works for at least one year during the second stretch of employment.

- Members of the contributory EPS or TPS receive eligibility service credit for prior service if: (1) the member separated from the first stretch of employment on or before June 30, 1998; (2) the member was not entitled to a vested benefit from the EPS or TPS at the time of separation; and (3) the member works for at least one year during the second stretch of employment.

- Members of the EPS and TPS must file for accidental disability benefits within two years of the end of membership (for a total of six years from the time of separation from employment).

Background and Current Law:

Break-in-Service Provisions

Break-in-service provisions provide for the retention of previous service credits if there is a period of separation from employment in a fiscal year after the one in which a member first becomes employed. As part of the 1998 pension enhancement legislation (HB 987, Chapter

530 of 1998), the break-in-service provisions were inadvertently eliminated for the new contributory EPS and TPS systems. As a result, a non-vested member of the contributory EPS or TPS immediately loses all prior service if the member terminates employment, however briefly.

Former Vested Members

Chapter 530 of 1998 specified that vested members who had left employment prior to July 1, 1998 did not receive the pension enhancement provided under the legislation. Some of these former vested members have since returned to State or local employment and have been enrolled in the contributory EPS or TPS. Under current law, when these former vested members return to employment with the State or other participating employers, they cannot combine their previous and new service credits.

The current rules impact returning former vested members in two ways. First, the average final compensation used for their first block of service will be based on their salary at their first termination, which would presumably be lower than their average final compensation at final retirement. Prior to the pension system enhancement, members could combine their blocks of service and apply their "final" average final compensation.

Second, the pension enhancement provided 1.2% of average final compensation for service before June 30, 1998. Previously, the formula was integrated with Social Security, but calculated in a way that it provided less than 1.1% for most members, and the calculated benefit was declining each year. This phenomenon will likely continue for all former vested members, including those who return to employment with the State or the participating employer.

State Expenditures: The proposed break-in-service provisions will have minimal impact on pension liabilities, and hence State contributions to the SRPS. The proposed withdrawal and redeposit provisions will also have a minimal impact because there would be no net loss of employer contributions. The only loss to the State would be the difference between 5% (the regular interest that the member must pay on redeposit of contributions) and 8% (the assumed actuarial return). The 3% difference in interest rate on the redeposited member contributions will have a minimal fiscal impact.

The proposed rules for former vested members will have an actuarial impact because the benefit for the vested member's former service will be at a higher accrual rate and will be based on a higher average final compensation. Because the actuary's valuation already reflects the cost of providing the higher average final compensation (and hence is included in the State valuation), that cost is not included in this estimate.

The State's actuary, Milliman & Robertson, estimates that providing the higher accrual rate on past service to former vested members who return to State employment will increase State pension liabilities by $16.7 million. These additional liabilities are amortized over 19 years (from fiscal 2002 through fiscal 2020), resulting in a first-year amortization payment of $1.1 million in fiscal 2002 and increasing 5% per year thereafter based on actuarial assumptions.

These estimates are based on the assumption that in fiscal 2000, 398 former vested members of the TPS will return to employment and receive credit for service before July 1, 1998 and 276 former vested State employee members of the EPS will return and receive similar credit. Each year thereafter, it is assumed that 20% fewer teachers and State employees will return to employment with service prior to July 1, 1998.

Of the $1.1 million in additional amortization payments, it is assumed that 100% of the TPS costs are general funds and 60% of the EPS costs are general funds. Twenty percent of the EPS costs are assumed to be special funds and 20% federal funds.

The State Retirement Agency advises that to implement the bill's changes, it will require an additional $50,000 in administrative expenses for combining accounts, refunding contributions, redepositing contributions, and re-crediting prior service. Legislative Services believes this estimate to be excessive and advises that the agency can implement these changes with existing resources. Legislative Services notes that the agency currently implements similar provisions for the "old" retirement systems and had previously implemented related provisions for the EPS and TPS before these provisions were inadvertently deleted.

Local Expenditures: For local governments that participate in the SRPS and that elected the enhancement, pension liabilities could increase by $2.0 million, resulting in additional amortization payments of $130,000 beginning in fiscal 2002 and increasing 5% per year thereafter based on actuarial assumptions. It is not possible to allocate these additional costs among the participating local governments.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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