HB 1453

Department of Legislative Services
Maryland General Assembly
2002 Session

FISCAL NOTE

House Bill 1453 (Chairman, Appropriations Committee)
Appropriations

Correctional Officers' Retirement System - Deferred Retirement Option Program

This pension bill creates a Deferred Retirement Option Program (DROP) for members of the Correctional Officers' Retirement System (CORS).

The bill takes effect July 1, 2002. DROP would go into effect if and when the Internal Revenue Service (IRS) issues an affirmative determination letter on DROP's effect on the pension system's tax qualified status.

Fiscal Summary

State Effect: State pension liabilities would increase by approximately $31.1 million, resulting in increased employer pension contributions of $1.8 million beginning in FY 2004 and increasing thereafter based on actuarial assumptions. One-time administrative expenses by the State Retirement Agency are estimated at $300,000 in FY 2003; ongoing administrative expenses are estimated at $30,000 per year.

(in dollars)	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
Revenues	$0	$0	$0	$0	$0
SF Expenditure	300,000	30,000	30,000	30,000	30,000
GF/SF/FF Exp.	0	1,820,000	2,000,000	2,190,000	2,400,000
Net Effect	($300,000)	($1,850,000)	($2,030,000)	($2,220,000)	($2,430,000)

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

Local Effect: None.

Small Business Effect: None.

Analysis

Bill Summary: The bill creates a DROP that, in general, allows CORS members to retire from CORS but continue to be employed by the State in the same position for a fixed period of time. The member's benefit payments (based on service credit and salary at "retirement") are maintained by the State pension system in a fictional account where the member earns interest and receives any cost-of-living adjustments (COLA) to the basic retirement allowance. The member does not accrue any additional service during the DROP period. At the end of the fixed period, the member terminates employment and receives the value of the DROP account and begins to receive the normal retirement allowance (including accrued COLAs) as well. The specifics of DROP are as follows:

- To be eligible for DROP, a member must have at least 20 years of service but less than 30 years of eligibility service.
- A member may participate in DROP for a period not to exceed the lesser of: (1) 5 years; (2) the difference between 30 years and the member's eligibility service as of the date of the member's election to participate in DROP and retire from CORS; or (3) a term selected by the member.
- When applying for DROP, the member must sign a binding letter of resignation specifying the member's date of termination.
- A DROP participant is officially a retiree of CORS even though the member continues to work. DROP participants would continue to be eligible for all other fringe benefits (such as health insurance) available to permanent State employees.
- The DROP member earns 6.0% (compounded monthly) on the member's retirement allowance paid during the DROP period.
- Upon termination of DROP, the member or designated beneficiary receives the DROP amount in a lump sum.
- The DROP member is eligible for death and accidental disability benefits even though the member has retired from CORS.

Implementation of DROP is contingent on an affirmative determination letter from the IRS (indicating, among other things, that DROP does not harm the tax-qualified status of CORS).

The bill also provides that CORS members who have 25 or more years of eligibility service as of July 1, 2002 will be provided a one-time, 6-month window of opportunity to elect to participate in DROP for a period not to exceed 5 years. The window of opportunity will commence on the first day of the month after the State Retirement Agency receives a favorable determination letter from the IRS.

Current Law: CORS is a "20 and out" plan that provides for 1.8% of average final compensation for each year of service. Members contribute 5% or 7% of pay, depending on the COLA that they elect.

Background: This bill is the product of collective bargaining. The State Police Retirement System includes a 4-year DROP beginning at 22 years of service. The Law Enforcement Officers' Pension System (LEOPS) includes a 5-year DROP beginning at 25 years of service. HB 1447 of 2002 seeks a 5-year DROP for members of the Employees' Retirement System and Employees' Pension System beginning at 30 years of service.

State Expenditures: As of June 30, 2001, there were 6,904 active members of CORS. It is estimated that as of July 1, 2002, there will be approximately 582 members of CORS who will have at least 20 years of eligibility service and be eligible for DROP. It is assumed that 90% of those eligible will elect DROP.

The State's actuary informally estimates that the proposal would increase State pension liabilities by approximately $31.1 million. Amortizing these liabilities over 25 years plus additional normal costs would result in increased State pension contributions of $1.8 million beginning in fiscal 2004. CORS pension costs are not reflected in a separate contribution rate; rather, they are subsumed within the employees' system. Because the actuary does not anticipate increasing the employees' system normal cost as a result of this legislation, unfunded liabilities will increase at more than the standard 5% per year actuarial assumption. Also, because CORS costs are subsumed in the general employees' rate, the additional costs will be dispersed among all State agencies.

Unlike DROPs for the State Police and LEOPS, which are sufficiently small to be processed manually, this program will require considerable computer programming, communications costs, and additional personnel expenditures. Special fund expenditures could increase by an estimated $300,000 in the first year following IRS approval. This estimate reflects the cost of hiring additional contractual fiscal personnel for six months to handle the initial surge of applications. It includes salaries, communications materials and postage, overtime expenses, computer reprogramming, and member seminars. Future year expenditures of approximately $30,000 per year reflect additional overtime and/or contractual personnel expenditures for ongoing administration of DROP.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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