

**Department of Legislative Services**  
 Maryland General Assembly  
 2005 Session

**FISCAL AND POLICY NOTE**  
**Revised**

House Bill 760  
 Appropriations

(Delegate Cadden, *et al.*)

Budget and Taxation

**Deferred Retirement Option Program - Eligibility**

This bill allows specified members of the State Police Retirement System (SPRS) to participate in the Deferred Retirement Option Program (DROP) retroactively or prospectively. The bill also allows specified members of the Law Enforcement Officers' Pension System (LEOPS) to participate in DROP retroactively. The bill also provides that 6% interest, compounded monthly, shall be applied to any DROP payments. The bill is effective July 1, 2005.

**Fiscal Summary**

**State Effect:** State pension liabilities could increase by \$5.4 million resulting in increased annual State pension contributions with a first year (2007) cost of \$322,700. Out-year costs reflect actuarial assumptions.

(in dollars)	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
Revenues	\$0	\$0	\$0	\$0	\$0
GF Expenditure	0	193,600	202,900	206,100	218,500
SF Expenditure	0	64,500	67,600	68,700	72,800
FF Expenditure	0	64,500	67,600	68,700	72,800
Net Effect	\$0	(\$322,600)	(\$338,100)	(\$343,500)	(\$364,100)

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

**Local Effect:** None.

**Small Business Effect:** None.

## Analysis

### Bill Summary:

#### *State Police Retirement System*

A member of SPRS may participate in DROP retroactively if the member: (1) is a member on July 1, 2005; (2) had accumulated more than 24 years of service as of July 1, 1999; and (3) is at least 57 years old but less than 60 years old on or before July 1, 2005.

The bill sets forth enrollment procedures and provides that the DROP period ends on the date the application for enrollment is submitted. The DROP period is to begin the lesser of three years or a term selected by the member, prior to submitting the application. For prospective enrollment in DROP, the same requirements apply, but a member need not be at least 57 years old. The period may run the lesser of three years or the difference between age 60 and the member's age as of the date of application.

For example, a 56 year old member may only enroll prospectively, for up to three years. However, a 57 year old member may enroll either prospectively or retroactively for no more than three years. Finally, a 58 year old member may enroll either retroactively for up to three years, or prospectively for up to two years.

#### *Law Enforcement Officers' Pension System*

The bill provides that a member of LEOPS may participate in DROP retroactively if the member: (1) is a member on July 1, 2005; (2) had accumulated more than 25 years of service as of July 1, 2000; and (3) is at least 56 years old on or before July 1, 2005. The bill provides that a member of LEOPS may enroll in DROP retroactively for a period of no more than four years.

**Current Law:** Under DROP, a member elects to technically "retire" but agrees to work for no more than a fixed additional period of service. The member receives pension benefits payments into an interest-bearing account held by the State Retirement Agency. When the DROP period ends and "true" retirement begins, the retiree receives a monthly retirement benefit based on the years of service and salary at the time the retiree entered DROP, plus a lump sum payment equal to the value of the DROP account.

Members of SPRS are eligible to participate in DROP if they have at least 22 and less than 28 years of eligibility service, and are less than 60 years old. Eligible members elect to participate for a period not greater than the lesser of: (1) four years; (2) the difference between 28 years and the eligibility service credit as of the date of election to participate

in DROP; (3) the difference between age 60 and the member's age as of the date of the member's election to participate in the DROP; or (4) a term selected by the member.

Members of LEOPS are eligible to participate in DROP if they have at least 25 and less than 30 years of eligible service. Eligible members elect to participate for a period not greater than the lesser of: (1) five years; (2) the difference between 30 years and the service credit accumulated as of the date of election to participate in DROP; or (3) a term selected by the member.

**Background:** DROP was established in statute by Chapter 122 of 1999, which required the Department of Budget and Management to seek approval of the proposed DROP program with the Internal Revenue Service (IRS). This approval took over a year to secure, and certain members of SPRS were subsequently excluded from participation in the DROP program. The program limits participation to no more than four years, governed by the member's age. While awaiting IRS approval for the DROP program, these members passed age 60 and were no longer eligible for DROP, despite accumulating the required service time.

**State Fiscal Effect:** The State Retirement Agency (SRA) and the State's actuary estimate that this bill would affect approximately 15 members of SPRS and 28 members of LEOPS with significant service who would, if allowed, participate in DROP.

#### *State Police Retirement System*

It is assumed that all 15 members will elect to join DROP, based on two factors: (1) SPRS allows members to earn only up to 28 years of service credit; and (2) the step increases in pay at that stage in an officer's career are relatively small. Based on this data, the State's actuary informally estimates that the bill would add \$3.0 million in SPRS liabilities, resulting in a first year (fiscal 2007) cost of \$182,700. This calculation assumes that eight officers would elect to join retroactively, and seven officers would elect to join prospectively.

#### *Law Enforcement Officers' Pension System*

It is estimated that 14 of 28 LEOPS members will elect to join DROP retroactively, based on the same reasons provided for members of SPRS. Based on this data, the State's actuary informally estimates that the bill would add \$2.4 million in LEOPS liabilities, resulting in a first year (fiscal 2007) cost of \$140,000.

### *Total Cost*

The bill will result in a total of \$5.4 million in new State pension liabilities. Amortizing these costs over 25 years results in a first year (fiscal 2007) employer cost of \$322,700. Out-year costs reflect actuarial assumptions.

Employer contributions would cover the cost of monthly allowance checks, accumulated cost-of-living adjustments, 6% compound interest, and a refund of employee contributions (with 4% interest) made into the system during the DROP period. Officers electing to join DROP retroactively are forfeiting the employer contributions made on their behalf, and the right to a higher benefit. The monthly benefit allowance for these officers is calculated as of the starting date of the DROP period, and as such is lower than it would be at present or moving forward.

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### **Additional Information**

**Prior Introductions:** Similar legislation was introduced in the 2004 session. HB 707 was unfavorably reported by the Appropriations Committee and SB 344 was unfavorably reported by the Budget and Taxation Committee.

**Cross File:** SB 1 is identified as a cross file but it is not identical.

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

**Fiscal Note History:** First Reader - February 16, 2005  
ncs/jr Revised - Correction - February 21, 2005  
Revised - House Third Reader - April 8, 2005  
Revised - Enrolled Bill - May 9, 2005

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