Department of Legislative Services

Maryland General Assembly
2008 Session

FISCAL AND POLICY NOTE

House Bill 1114 (Delegates Waldstreicher and Levy)
Appropriations

Optional Defined Contribution System - Enrollment and Participation

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This bill automatically enrolls new members of the Employees' Pension System (EPS) in a targeted retirement fund offered by the Maryland Supplemental Retirement Plan (MSRP) and automatically deducts a $23 employee contribution per pay period from their compensation. The automatic enrollment provision is contingent on MSRP offering targeted retirement funds as investment options to its members. Employees eligible for the automatic enrollment and deduction may elect to opt out.

The bill takes effect July 1, 2008 and applies only prospectively to employees hired after that date.

Fiscal Summary

State Effect: State expenditures (all funds) increase by $1.48 million in FY 2009 to pay the State matching contribution for State employees automatically enrolled in MSRP. Out-year estimates reflect cumulative growth as new employees are added to the plans each year. Personnel costs are assumed to be split 60% general funds, 20% special funds, and 20% federal funds. Special fund revenues for MSRP also increase by an indeterminate amount due to the increase in assets invested in the plans.

(in dollars)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
SF Revenue	-	-	-	-	-
GF Expenditure	888,000	1,776,000	2,664,000	3,552,000	4,440,000
SF Expenditure	296,000	592,000	888,000	1,184,000	1,480,000
FF Expenditure	296,000	592,000	888,000	1,184,000	1,480,000
Net Effect	($1,480,000)	($2,960,000)	($4,440,000)	($5,920,000)	($7,400,000)

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

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law: The Board of Trustees of the Teachers' and State Employees' Supplemental Retirement Plans administers three deferred compensation plans and an employer matching program on behalf of State employees. MSRP staff provide education programs and support to State employees and human resource personnel in State agencies, and assist the board in the selection of investment options. MSRP finances its operations through a fee imposed on its members' accounts, based on a percentage of assets in the plans. For fiscal 2008 and 2009, the board fee is 0.05% of assets. In addition, the board contracts with Nationwide Retirement Solutions, Inc., for administration of all four plans. Beginning in fiscal 2009, Nationwide's administration fee will be 0.14%, so the combined asset fee paid by participants is 0.19%.

Participation in the MSRP plans is voluntary for eligible employees. State employees who participate in MSRP and who are members of EPS are entitled to an employer matching contribution up to $600 per year. The match was suspended in fiscal 2004 and 2005 for budgetary reasons and was reinstated at a maximum level of $400 for fiscal 2006. Beginning in fiscal 2007, the match has remained at its statutory maximum of $600.

The federal Pension Protection Act of 2006 provided administrative incentives for administrators of defined contribution plans to adopt automatic enrollment policies for new employees.

Background: MSRP offers an array of investment options to its members, including a money market fund, bond funds, and a mixture of domestic and international equity mutual funds. In February 2007, the board unveiled a family of life cycle funds, also called targeted retirement funds. Administered by T. Rowe Price, the life cycle funds are mutual funds that feature an asset mix that adjusts over time as the individual investor ages. The board opted to include life cycle funds because its own research showed that more than half of its members had not adjusted their asset allocation for more than two years. With life cycle funds, asset allocation is handled by the fund managers, so members in essence receive investment management services for the same fees they currently pay to individual mutual fund managers. Life cycle funds are growing in popularity among defined contribution programs and are already offered by the Maryland College Savings Plan.

These options have quickly become a popular vehicle for retirement investing. **Exhibit 1** shows the 12 different funds T. Rowe Price offers and the total plan assets held in each fund as of September 30, 2007. In less than a year, the life cycle funds have registered $60,252,805 in retirement contributions, or 2.4% of the entire MSRP portfolio. In the quarter ended September 30, 2007, 9.4% of plan contributions were invested in life cycle funds.

Exhibit 1
T. Rowe Price Life Cycle Fund Offerings
Asset Holdings as of September 30, 2007

Fund	Assets	% of Total
2005 Fund	$2,517,393	4.2%
2010 Fund	9,473,572	15.7%
2015 Fund	14,076,336	23.4%
2020 Fund	11,990,733	19.9%
2025 Fund	8,040,541	13.3%
2030 Fund	6,312,154	10.5%
2035 Fund	3,126,886	5.2%
2040 Fund	2,455,119	4.1%
2045 Fund	596,358	1.0%
2050 Fund	465,279	0.8%
2055 Fund	308,933	0.5%
Income Fund	889,501	1.5%
Total	**$60,252,805**	

Source: Nationwide Investments *Administrator's Report* 3rd Quarter 2007

State Fiscal Effect: Based on data provided by the State Retirement Agency, Legislative Services estimates that approximately 6,250 new State employees enroll in EPS each year. In fiscal 2007, 75% of eligible employees enrolled in MSRP, and 69% of them actively deferred a portion of their compensation. However, that figure includes employees who are not eligible for the State match because they are not members of EPS. Presumably, the proportion of EPS members who defer to one or more accounts is slightly higher because of the incentive provided by the match. Assuming that 75% of State employees who participate in MSRP actively defer, 56% of eligible State employees would participate in MSRP *and* defer to an account in the absence of this bill. Therefore, it is assumed that 2,750 new State employees (44%) would be subject to automatic enrollment in the targeted retirement funds offered by MSRP each year.

Assuming that 10% of those employees opt out of the program, that leaves 2,475 new employees who would be subject to automatic enrollment. The $23 automatic deduction per pay period entitles them to a State match of $598. Therefore, State expenditures would increase by $1.48 million in fiscal 2009. That figure would increase cumulatively as new State employees were hired in succeeding years, yielding a total increase of $7.4 million by fiscal 2013. Those costs are presumed to be split 60% general funds, 20% special funds, and 20% federal funds.

Special fund revenues would increase for MSRP based on increased participation in the plans and its 0.05% administrative fee. The amount of the increase cannot be reliably estimated because it is based on assets held in the plans. Plan assets vary according to market conditions, and some employees may elect to contribute more than the minimum $23 contribution per pay period. However, the increase could be considerable and likely result in a reduction of the administrative fee.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Maryland Supplemental Retirement Plans, Maryland State Retirement Agency, Department of Legislative Services

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mll/jr

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