

Department of Legislative Services
Maryland General Assembly
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FISCAL AND POLICY NOTE
Revised

House Bill 1585
Appropriations

(Delegate Griffith, *et al.*)

Budget and Taxation

Local Governments - Postemployment Benefits - Investment of Funds

This bill authorizes local governments to contract with external asset managers to manage or invest money designated for other postemployment benefits (OPEB) besides employee pensions. It further authorizes local governments to create pooled OPEB investment funds with separate accounts for each local government that participates in the fund, and to remit funds intended for OPEB to the Treasurer for investment in the Local Government Investment Pool.

Fiscal Summary

State Effect: None.

Local Effect: Local government revenues from investment earnings for OPEB benefits could increase by an indeterminate amount to the extent that local governments form OPEB investment pools. Local government expenditures for asset management services could also increase, but should be more than offset by investment earnings.

Small Business Effect: None.

Analysis

Current Law: Chapter 543 of 2006 allows local governments to invest, redeem, sell, exchange, and reinvest funds dedicated to paying postemployment benefits in the same manner that they invest funds for employee pensions. Postemployment benefits are defined as health care benefits for retirees and all other postemployment benefits except pensions. Funds dedicated to paying for postemployment benefits are excluded from the statutory definition of “public funds” for the purpose of restricting their investment.

Except for funds invested for the purpose of funding pension and other postemployment benefits, local government investment policies must abide by the same restrictions applied to investments made by the State Treasurer. Therefore, they may invest only in low-risk investment options, including:

- U.S. Treasury bills;
- bonds and commercial paper with the highest quality letter and numerical rating by at least one rating agency;
- money market funds; and
- the Maryland Local Government Investment Pool.

Background: Statements 43 and 45 from the Government Accounting Standards Board (GASB) require governmental employers to include in their 2008 financial statements any liabilities associated with the commitments they have made to provide postemployment benefits other than pensions. These other postemployment benefits include health insurance for retirees, as well as any life insurance or long-term care insurance paid by the employer. For public employers that offer subsidized health insurance to their retirees, OPEB liabilities can be substantial. For instance, a 2007 actuarial analysis found that the State of Maryland's OPEB liabilities exceed \$15 billion. **Exhibit 1** provides OPEB liabilities and annual required contributions for all county governments.

Exhibit 1
OPEB Liabilities in Maryland Counties
(\$ in Millions)

	OPEB Liability	Annual Required Contribution	County	Includes:		
				Teachers	Libraries	Comm. College
Allegany	\$37.3	\$3.6	√			
Anne Arundel	1,270.0	117.6	√	√	√	√
Baltimore City	NA	NA				
Baltimore	1,800.0	150.0	√	√	√	√
Calvert	154.1	13.3	√	√		
Caroline	73.5	6.7	√	√		
Carroll	266.8	17.1	√	√	√	
Cecil	45.8	4.3	√	√		
Charles	386.2	36.8	√	√		
Dorchester	20.4	2.2	√			
Frederick	416.7	44.3	√	√	√	
Garrett	46.6	3.0	√	√		√
Harford	457.7	47.0	√	√	√	
Howard	476.6	53.0	√	√	√	√
Kent	NA	NA				
Montgomery	2,600.0	240.0	√	√	√	√
Prince George's	2,170.0	85.0	√	√	√	√
Queen Anne's	66.3	6.6	√	√		
St. Mary's	214.0	12.8	√	√	√	
Somerset	NA	NA				
Talbot	NA	NA				
Washington	135.8	10.7	√	√		
Wicomico	74.4	5.0	√	√		
Worcester	121.6	17.0	√	√		

Source: Maryland Association of Counties

Most employers pay for OPEB on a pay-as-you-go basis, which means that they only pay for actual costs (*e.g.*, insurance premiums) incurred by their retired members in a given year. However, if they have made a commitment to provide health insurance or other postemployment benefits to current employees when they retire, the employers continue to accumulate liabilities to pay for those benefits in the future. Unless the employers set aside money now to cover those future costs (known as prefunding), those liabilities add up each year, and GASB is now requiring employers to calculate the value of those future liabilities and account for them on their financial statements. Although GASB is not requiring employers to prefund OPEB liabilities, OPEB liabilities that appear on public employers' accounting statements can hurt their bond ratings, making it more expensive for them to borrow money.

Therefore, many public employers are exploring options for prefunding their OPEB liabilities, including establishing separate OPEB funds similar to their pension funds. Since the early 1990s, when GASB changed the accounting rules for pension funds, most public employers have been prefunding their pension liabilities. Typically, they set aside money in a pension fund each year to cover all or most of the liability they incur each year for the future pension benefits of their current employees. This allows them to invest that money in the hopes of earning a significant return to help them cover their future costs.

Many jurisdictions, however, do not have the resources to manage their own investment portfolios. Many participate in the Local Government Investment Pool managed by the Treasurer's Office to manage their regular investments, but there is no equivalent pool to manage OPEB investments. OPEB funds can be invested in a broader range of investment vehicles and, therefore, require even more investment expertise.

Local Fiscal Effect: By allowing local governments to form OPEB investment pools and contract with external asset managers, the bill allows local governments to take full advantage of the flexibility provided by Chapter 543 of 2006 to invest in equities and other high-yield, high-risk assets. This could increase the investment returns they earn on the funds they choose to set aside to prefund their OPEB obligations.

Additional Information

Prior Introductions: None.

Cross File: SB 945 (Senator Kasemeyer) – Budget and Taxation.

Information Source(s): Wicomico County, Allegany County, Montgomery County, Prince George's County, Talbot County, Treasurer's Office, Department of Budget and Management, Maryland Association of Counties, Department of Legislative Services

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Analysis by: Michael C. Rubenstein

Direct Inquiries to:
(410) 946-5510
(301) 970-5510