Department of Legislative Services

Maryland General Assembly
2008 Session

FISCAL AND POLICY NOTE

House Bill 817 (Delegate Barkley)
Appropriations

Retirement and Pensions - Service Retirement Allowances

This bill allows members of the Teachers' Pension System and Employees' Pension System who have prior service credit in either the Teachers' Retirement System or the Employees' Retirement System to choose whether to have their ERS/TRS allowance calculated using the TRS/ERS formula in effect at the time they transferred to TPS/EPS, or to merge their prior service credit with their TPS/EPS credit and have their benefits calculated under the TPS/EPS formula.

The bill takes effect July 1, 2008.

Fiscal Summary

State Effect: State pension liabilities could increase by $248,000 and normal costs could increase by $1,588,000. Amortizing the liabilities over 25 years and adding the normal cost yields a first year cost of $1,661,000 in fiscal 2010. This is assumed to increase annually according to actuarial assumptions. The costs associated with TPS members are paid entirely with general funds, while the costs associated with EPS members are assumed to be split 60% general funds, 20% special funds, and 20% federal funds.

Revenues	$0	$0	$0	$0	$0
($ in thousands)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
GF Expenditure	$0	$1,369	$1,416	$1,466	$1,517
SF Expenditure	0	146	151	157	162
FF Expenditure	0	146	151	157	162
Net Effect	$0	($1,661)	($1,719)	($1,779)	($1,841)

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

Local Effect: None.

Small Business Effect: None.

Analysis

Bill Summary: Members who choose to merge prior service credit in TRS/ERS with TPS/EPS credit would have their benefits calculated according to the TPS/EPS formula. Therefore, any credit earned under TRS/ERS would be applied to the retirement allowance using the TPS/EPS accrual rate in effect at the time the credit was earned. The member's average final compensation (AFC) at the time of retirement would be applied to all service credit. Retiring members who choose this option would not be entitled to any refund of the portion of their ERS/TRS employee contributions that exceeded the TPS/EPS employee contributions in effect at the time.

Members who choose not to merge their prior credit with their current credit would continue to have their allowances calculated separately. The retirement allowance based on service credit earned under TRS/ERS would be calculated using the benefit formula and average final salary in effect under TRS/ERS at the time they transferred to TPS/EPS. The retirement allowance based on service credit earned under TPS/EPS would be calculated using the benefit formula and AFC in effect at the time of retirement, then added to the TRS/ERS benefit.

Current Law: Retirement allowances for normal service retirees of TPS/EPS with prior service credit in TRS/ERS are calculated separately. The retirement allowance based on service credit earned under TRS/ERS is calculated using the benefit formula and average final salary in effect under TRS/ERS at the time of the member's transfer to TPS/EPS. The retirement allowance based on service credit earned under TPS/EPS is calculated using the benefit formula and AFC in effect at the time of retirement, then added to the TRS/ERS benefit.

The TRS/ERS retirement benefit formula provides 1.8% of average final salary for each year of service. The required employee contribution is 5% of compensation for members who choose to be subject to a 5% cap on annual cost-of living-adjustments (COLAs) based on the Consumer Price Index for Urban Consumers (CPI-U), or 7% for members who choose unlimited COLAs. Average final salary is defined as the average of the member's highest three years' compensation.

TPS/EPS members earn a retirement benefit allowance according to the following formula:

Years of Creditable Service Before 1998	x	AFC	x	1.2%

Plus

Years of Creditable Service After 1998	x	AFC	x	1.8%

AFC is defined as the average of the member's compensation for the final three years of employment. Prior to 1998, TPS/EPS was noncontributory for members. From 1998 to 2006, the employee contribution rate was 2% of the member's compensation. Chapter 110 of 2006 raised employee contributions to 5%, phased in over three years. TPS/EPS retirees earn COLAs equal to CPI-U, subject to a 3% cap.

Background: TRS/ERS were closed to new members in 1980 and replaced by TPS/EPS for all new hires. Prior to January 1, 2005, TRS/ERS members could transfer to the newer systems and receive a refund of all accumulated employee contributions with interest, but if they transferred after April 1, 1998, they were not eligible for TPS/EPS benefit enhancements enacted in 1998 and 2006.

State Fiscal Effect: The State Retirement Agency has identified 282 active TPS/EPS accounts where a member has a vested benefit in TRS/ERS, respectively. Of those, 158 TPS members have vested TRS accounts with an average of 10 years of service credit, and 124 EPS members have ERS accounts with an average of 11.9 years of service credit. Their average age is 56.

The most significant impact on benefits would be for employees whose average final compensation as a member of TPS/EPS is significantly higher than the average final salary used to determine their benefits for their prior service with TRS/ERS. This would help overcome the use of the lower 1.2% multiplier that would be applied to the TRS/ERS service.

In calculating the cost of this analysis, Legislative Services and the General Assembly's actuary made two assumptions. First, based on the service and compensation records of the 282 affected individuals, it was assumed that all affected individuals would choose to transfer their TRS/ERS credit to TPS/EPS. Second, Legislative Services and the General Assembly's actuary assumed that the full cost of these transfers would be accounted for in the June 30, 2008 actuarial valuation. This is standard practice in all DLS analyses of pension benefit changes. As a result, the bulk of the increased cost would be allocated to normal cost, which is recognized over the members' remaining years of employment. Given the members' average age, that represents between 2 and 10 years. However, if the system's actuary waits to recognize the cost of the transfer until each member retires, the bulk of the cost would be allocated to actuarial accrued liability and be amortized over 25 years. That would reduce the annual employer contribution by spreading the cost out over a longer timeframe.

Applying the DLS assumptions, State pension liabilities increase by $248,000 and normal costs increase by $1,588,000. Amortizing the liabilities over 25 years and adding the normal cost yields a first year cost of $1,661,000 in fiscal 2010. This is assumed to increase annually according to actuarial assumptions, but the bulk of the cost would end as soon as the last affected member retired. The costs associated with TPS members (56% of the total) are paid entirely with general funds, while the costs associated with EPS members are assumed to be split 60% general funds, 20% special funds, and 20% federal funds.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): State Retirement Agency, Mercer Human Resources Consulting, Inc., Department of Legislative Services

Fiscal Note History: First Reader - February 17, 2008
mcp/jr

Analysis by: Michael C. Rubenstein

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