

Department of Legislative Services  
 Maryland General Assembly  
 2008 Session

FISCAL AND POLICY NOTE

House Bill 798 (Delegate Niemann)  
 Appropriations

State Personnel and Pensions - Contractual Employees - Health Benefits and  
 Purchase of Service Credit

This bill makes contractual State employees who have worked for the State for at least six months eligible for subsidized health benefits under the State Employee and Retiree Health and Welfare Benefits Program (State plan). For members of the Employees' Pension System (EPS), the bill lowers the cost of purchasing service credit for periods of contractual full-time employment with the State.

The bill takes effect July 1, 2008.

Fiscal Summary

**State Effect:** State expenditures could increase by \$217.8 million in fiscal 2009 to provide subsidized health coverage to participating contractual employees. Out-year expenditures reflect a 9% medical cost inflation and a constant number of contractual employees receiving subsidized health benefits. In addition, State pension liabilities could increase by \$22.4 million and normal costs by \$1.8 million. Amortizing the liabilities over 25 years and adding the normal costs results in State pension contributions increasing by \$3.2 million in fiscal 2010 (first year). Those costs are assumed to increase annually according to actuarial assumptions. All costs are assumed to be split 60% general funds, 20% special funds, and 20% federal funds.

(\$ in millions)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Revenues	\$0	\$0	\$0	\$0	\$0
GF Expenditure	130.7	144.4	157.3	171.3	186.7
SF Expenditure	43.6	48.1	52.4	57.1	62.2
FF Expenditure	43.6	48.1	52.4	57.1	62.2
Net Effect	(\$217.8)	(\$240.7)	(\$262.2)	(\$285.6)	(\$311.1)

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

**Local Effect:** Total pension liabilities for participating governmental units (PGUs) increase by \$7.7 million and normal costs increase by \$744,000. Amortizing the liabilities over 25 years and adding the normal costs yields a first year increase in PGU pension contributions of \$1.2 million. Those costs are assumed to increase annually according to actuarial assumptions

**Small Business Effect:** None.

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## Analysis

**Bill Summary:** Members of the Employees Retirement System and EPS who purchase service credit for past contractual full-time employment must pay, in a single payment, the employee contribution that the member would have been required to pay at the time of contractual employment, plus 4% (for ERS) or 5% (for EPS) regular interest. They may purchase service credit for past contractual employment at any time prior to retirement. This changes the cost formula for EPS members but retains the formula currently in place for ERS members.

**Current Law:** *Subsidized Health Benefits.* A contractual employee is an individual who provides temporary personal services to the State for pay and who is not employed in a budgeted position. A contractual employee may enroll in the State plan; however, the employee must pay the total cost of the premium and may not receive a State subsidy.

Regular State employees may enroll in the State plan and receive a State subsidy of either 80% or 85% of their premium, depending on the coverage option they select.

*Purchase of Pension Service.* At any time before retirement, ERS members may purchase service credit at member cost for past employment:

- with the State or a participating governmental unit (including contractual employment);
- as a member of the State Police Retirement System for which the member did not vest with that pension plan;
- when the member was on employer-approved leave not exceeding two years;
- with the Department of Legislative Services, the Office of the Attorney General, or as secretary to either the Speaker of the House of Delegates or the President of the Senate during a session of the General Assembly;
- as a member of the Senate or House of Delegates or the Office of the Secretary of the Senate or the Chief Clerk of the House of Delegates;

- as a member of ERS or the Teachers' Retirement System for which the member had withdrawn all accumulated contributions after a prior termination of membership; or
- when membership was mandatory but for which member contributions were not made.

EPS members may purchase service credit at full cost (both employee and employer share) for prior employment with the State (including contractual employment), a political subdivision of the State or of another state, the federal government, or a school or postsecondary institution. However, EPS members who are State employees pay only 50% of the full cost of the purchase, meaning that only employees of PGUs pay the full cost. All EPS service credit purchases may be made only in the year of retirement.

**State Expenditures:** *Subsidized Health Benefits.* The State's Central Payroll bureau reports that 9,878 contractual employees were paid on February 5, 2008. This figure includes all State agencies, including the Legislative and Executive branches, but does not include the University System of Maryland (USM), which manages its own payroll. Contractual employment varies seasonally, but is highest in the winter months when the General Assembly is in session.

In its payroll reports, USM does not distinguish between regular and contractual employees, but the Governor's proposed fiscal 2009 budget authorizes 6,177 contractual positions for public institutions of higher education. Assuming a ratio of 3:1 of contractual employees to contractual positions (as is the case across all other branches of State government), Legislative Services estimates that USM has 18,531 contractual employees. This yields a total count of 28,409 contractual employees in State government.

The bill specifies that only contractual employees who have worked for the State for six months are eligible for subsidized health coverage. Although contractual employment tends to be seasonal, the bill does not specify that the six months have to be consecutive. Legislative Services assumes that 80% of contractual employees meet the six-month threshold, for a total of 22,727 contractual employees eligible for subsidized health benefits.

DBM reports that the average annual State subsidy is \$10,650 per employee in the State plan. Assuming that 90% of eligible contractual employees elect to participate in the State plan, as is the case with regular State employees, approximately 20,454 contractual employees could enroll in the State plan. This analysis assumes that each employee would be eligible for a full year of coverage. Therefore, State expenditures could increase by \$217.8 million in fiscal 2009 to provide subsidized health coverage to participating contractual employees. These expenditures are assumed to be split 60%

general funds, 20% special funds, and 20% federal funds. Out-year expenditures reflect a 9% inflation rate for medical costs and a constant number of contractual employees being enrolled in the State plan.

*Purchase of Pension Service:* There is no reliable way to estimate the number of current ERS/EPS members who were previously employed as contractual employees by the State. The State Retirement and Pension System (SRPS) only maintains employment records for members; since contractual employees are not members, it has no records of their past contractual employment. Therefore, for the purpose of this analysis, Legislative Services assumes that 5% of active ERS and EPS members were previously employed as contractual employees. For EPS, it is also assumed that 0.5% of those members would have purchased past contractual service anyway, so the cost to the State generated by their service purchase under this bill is the difference between the current cost and the new cost. The remaining 4.5% of EPS members would not have purchased past service due to the prohibitive cost of paying either full cost or 50% of full cost. Finally, Legislative Services assumes that, on average, an eligible member will purchase two years of past contractual service.

Based on these assumptions, the General Assembly's actuary estimates that State pension liabilities would increase by \$22.4 million and normal costs would increase by \$1.8 million. Amortizing the liabilities over 25 years and adding the normal costs results in State pension contributions increasing by \$3.2 million in fiscal 2010. Those costs are assumed to increase annually according to actuarial assumptions and to be split 60% general funds, 20% special funds, and 20% federal funds.

**Local Expenditures:** Using the same assumptions, total pension liabilities for PGUs increase by \$7.7 million and normal costs increase by \$744,000. Amortizing the liabilities over 25 years and adding the normal costs yields a first year increase in PGU pension contributions of \$1.2 million. Those costs are assumed to increase annually according to actuarial assumptions.

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### **Additional Information**

**Prior Introductions:** None.

**Cross File:** None.

**Information Source(s):** Comptroller's Office, Mercer Human Resources Consulting, Maryland State Retirement Agency, Department of Budget and Management, Department of Legislative Services

**Fiscal Note History:** First Reader - February 17, 2008  
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