

Department of Legislative Services
Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

House Bill 886

(Delegate Olszewski, *et al.*)

Appropriations

Optional Defined Contribution System - Enrollment and Participation

This bill requires new members of the Employees' Pension System (EPS) to actively choose between enrolling or not enrolling in a targeted retirement fund offered by the Maryland Supplemental Retirement Plans (MSRP) at the time of EPS enrollment. In years in which the State provides an employer matching contribution, an enrollee must contribute at least one twenty-sixth of the matching contribution to the targeted fund. In years in which the State does not provide a matching contribution, the enrollee must contribute at least 1.5% of eligible compensation to the targeted fund.

The bill takes effect July 1, 2009, and applies only prospectively to employees who enroll in EPS after that date.

Fiscal Summary

State Effect: None. The bill does not result in increased participation in – or deferrals to – MSRP accounts by EPS members. Therefore, there is no effect on State expenditures for the State matching program.

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 resources 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. Since fiscal 2008, 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 is 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. However, the Governor's proposed fiscal 2010 budget does not include funding for the match.

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 are becoming a popular vehicle for retirement investing. **Exhibit 1** shows the 12 different funds T. Rowe Price offers through MSRP and the total plan assets held in each fund as of December 31, 2008. As of that date, the life cycle funds held \$80.8 million in assets, or 4.2% of the entire MSRP portfolio.

Legislative Services notes that employees may change their asset allocation multiple times in a single year, without penalty, among the different investment options offered by MSRP. Even though the bill requires that new employees accept or decline enrollment in a targeted fund, those who choose to participate may change their allocation to other investment options offered by MSRP after enrollment.

Exhibit 1
T. Rowe Price Life Cycle Funds
Asset Holdings (Unaudited) as of December 31, 2008

<u>Fund</u>	<u>Assets</u>	<u>% of Total</u>
2005 Fund	\$2,994,407	0.16%
2010 Fund	11,486,674	0.60
2015 Fund	15,929,290	0.83
2020 Fund	17,401,249	0.90
2025 Fund	11,373,148	0.59
2030 Fund	9,202,659	0.48
2035 Fund	4,783,742	0.25
2040 Fund	3,544,004	0.18
2045 Fund	1,443,220	0.07
2050 Fund	591,752	0.03
2055 Fund	352,293	0.02
Income Fund	1,698,252	0.09
Total	\$80,800,690	4.19%

Source: Maryland Supplemental Retirement Plans

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 2008, 73% of eligible employees participated in MSRP (*i.e.*, they have an active account but may or may not make contributions to the account), and 68% of them actively contributed a portion of their compensation to one or more of their accounts. 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 contribute 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 contribute, approximately 55% of eligible EPS members participate in MSRP *and* contribute to an account.

New State employees are currently provided with the opportunity to enroll in MSRP during their initial orientation. There are no additional incentives in the bill to encourage new EPS members to enroll, so there is no reason to believe that participation rates in the targeted funds will increase as a result of this bill. In fact, given the severity of recent financial market losses, and the absence of an employer match in fiscal 2010, participation rates may actually decline. Although the bill effectively increases the

minimum contribution from \$5 to \$23 per pay period in years when the State provides a fully funded employer match (one twenty-sixth of \$600), Legislative Services believes that most members contribute at least that amount in order to secure the full match. Therefore, there is no effect on State expenditures in years when the State provides an employer match.

Additional Information

Prior Introductions: HB 1114 of 2008 contained similar provisions. It was heard by the House Appropriations Committee and subsequently withdrawn.

Cross File: None.

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

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