SB 648

Department of Legislative Services

Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

Senate Bill 648 (Senators Pipkin and Brinkley)
Budget and Taxation

State Retirement and Pension System - Employer Contributions - Educators and Educational Staff

This bill requires each county government to pay a portion of the employer pension contribution for members of the Teachers' Retirement System (TRS) or Teachers' Pension System (TPS) who are employed by the county. It also expands the membership of the Board of Trustees of the State Retirement and Pension System (SRPS) to include representatives of local school boards and community colleges.

The bill takes effect July 1, 2009.

Fiscal Summary

State Effect: State general fund expenditures for employer pension contributions decrease by $100.2 million in FY 2011, representing the difference between total employer contributions of $813.0 million in FY 2010 for local TRS/TPS members and projected payments of $913.2 million in FY 2011. Out-year projections reflect growth in employer pension contributions based on actuarial assumptions.

(in dollars)	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
Revenues	$0	$0	$0	$0	$0
GF Expenditure	0	(100,185,500)	(210,233,400)	(318,718,900)	(452,690,200)
Net Effect	$0	$100,185,500	$210,233,400	$318,718,900	$452,690,200

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

Local Effect: Expenditures by county governments increase by a total of $100.2 million in FY 2011 to pay the local share of employer contributions for TRS/TPS members. Local government expenditures grow annually according to actuarial assumptions. **This bill imposes a mandate on a unit of local government.**

Small Business Effect: None.

Analysis

Bill Summary: Beginning July 1, 2010, each county government, including Baltimore City, pays annually the portion of the employer contribution for TRS/TPS members employed by the county that exceeds the total employer contribution calculated for fiscal 2010, until the local share reaches 50% of the total employer contribution. Thereafter, the State and local shares remain evenly divided.

The bill applies to TRS/TPS members who are employed by a county board of education as a clerk, helping teacher, teacher, principal, superintendent, or supervisor; librarians or clerical employees of a local public library; or faculty, professional, or clerical employees of a local community college.

For a regional community college, the local share of the employer pension contribution for community college faculty and staff is prorated among the counties that support the college. The prorated amounts are based on the proportion of full-time equivalent students enrolled at the college who reside in each county.

The State continues to pay the full employer contribution for TRS/TPS members who are:

- employed by Baltimore City Community College;
- faculty members employed by educational institutions supported and controlled by the State; or
- staff members of the University System of Maryland, Morgan State University, or St. Mary's College of Maryland and who were members of TPS as of January 1, 1998 or who transferred from TRS to TPS on or after that date.

Each year, counties must pay their share of the TRS/TPS employer contribution within 30 days of receiving certified contribution rates from the SRPS board, subject to a grace period of no more than 10 days at the discretion of the board's secretary. Failure to pay within 30 days or to secure a grace period results in a 10% penalty and 10% annual interest on the delinquent amount. If notified by the board's secretary that a delinquency exists for a particular county, the Comptroller must exercise the right of setoff against any money due or coming due to that county from the State.

Membership of the SRPS board expands from 14 to 15 members, with the additional member appointed by the board of directors of the Maryland Association of Counties

(MACo) to represent the interests of local school boards and community colleges. When the local share of the TRS/TPS employer contribution reaches 50% of the total employer contribution, the board expands to 17 members, with the 2 additional members also appointed by MACo to represent the interests of local school boards and community colleges.

Current Law: The State pays the full employer contribution for all TRS/TPS members, including employees of local boards of education, libraries, and community colleges.

Membership in TRS/TPS includes:

- employees of a day school in the State under the authority and supervision of a county board of education or the Baltimore City Board of School Commissioners;
- faculty employees of an educational institution supported and controlled by the State;
- librarians and clerical employees of local libraries;
- community college faculty and staff;
- staff members of the University System of Maryland, Morgan State University, or St. Mary's College of Maryland as of January 1, 1998; and
- nonfaculty employees of the Baltimore City Community College, prior to October 1, 2002.

The Board of Trustees of the State Retirement and Pension System consists of 14 members, including:

- 3 *ex officio* members (the Treasurer, Comptroller, and Secretary of Budget and Management);
- 5 members elected by members and retirees of the system's plans; and
- 6 members appointed by the Governor, including 1 member who represents the interests of local governments who participate in the system.

Background: Depending on their date of hire, membership in either TRS or TPS is mandatory for all State and local teachers and certain board of education, local library, and community college employees (except those eligible to participate in the Optional Retirement Program). TRS was closed to new membership in 1980 due to funding issues and replaced by TPS. TRS members are eligible for normal service retirement at age 60 or with 30 years of service regardless of age. TRS provides a normal service retirement benefit equal to one-fifty-fifth (1.818%) of average final compensation for each year of service. Members pay either a 5% or 7% contribution, depending on which cost-of-living adjustment (COLA) option they choose. Automatic COLAs are based on the Consumer

Price Index (CPI); members paying 5% are subject to a 5% cap, but members paying 7% are not subject to a cap. CPI has not exceeded 5% since 1991.

TPS members are eligible for normal service retirement at age 62 with 5 years of service or with 30 years of service regardless of age. From its inception in 1980 until 1998, TPS was noncontributory, so members paid nothing. From 1998 until 2006, members contributed 2%; Chapter 110 of 2006 phased in higher employee contributions until they reached the maximum 5% contribution in fiscal 2009. TPS provides a normal service retirement benefit equal to 1.2% of average final compensation for service credit earned prior to 1998 and 1.8% for service credit since 1998. Automatic COLAs are based on CPI, subject to a 3% cap.

As of June 30, 2008, TRS/TPS had a combined total of 105,982 active members, of whom only 4,125 were TRS members. **Exhibit 1** shows total membership by employer in fiscal 2009.

Exhibit 1
Fiscal 2009 TRS/TPS Membership, by Employer

	Members	**% of Total**
School Boards	97,406	91.9%
Community Colleges	4,392	4.1%
Libraries	2,356	2.2%
State Institutions	1,828	1.7%

Note: Percentages do not add to 100 due to rounding.
Source: State Retirement and Pension System

For actuarial purposes, the two teachers' systems are combined and the employer contribution is identical for both plans. The combined teachers' plans are subject to the corridor funding method, which was enacted by Chapter 440 of 2002 to mitigate the effects of fluctuations in market returns on employer contributions by spreading out those effects over five years. The corridor method froze employer contribution rates at 2002 levels as long as the plans remain actuarially funded between 90% and 110%. As the plans fall out of the corridor, the employer contribution increases by an amount equal to one-fifth of the difference between the prior year's rate and the "true" rate required to fully fund the system. The teachers' plans fell out of the corridor in fiscal 2006.

Of the 34 states that recently responded to a national survey, 31 require local governments to pay all or some of the employer pension contribution for teachers. Of those, 15 require local governments to pay the full employer's contribution with no support from the state. Only 3 of the 34 states – Maryland, Texas, and Kansas – pay the full employer contribution for teachers.

State Fiscal Effect: Employer contribution rates for TRS/TPS are determined annually by the SRPS actuary, based on actuarial assumptions established by the board and subject to the requirements of the corridor funding method. The projected fiscal 2010 employer contribution of $832.6 million for the combined teachers' systems is 63.1% higher than the fiscal 2007 contribution of $510.5 million. Rapid growth in the employer contribution rate has been driven largely by three factors:

- **negative investment returns in fiscal 2001, 2002, and 2008** – to mitigate against dramatic spikes in financial markets, the board spreads out, or smoothes, investment returns over five years, so the earlier losses affected contribution rates until 2007;
- **the benefit enhancement enacted by Chapter 110 of 2006** – the enhancement, which is not subject to the corridor method, increased the benefit multiplier for members of TPS and the Employees' Pension System from 1.4% to 1.8% for service credit earned since 1998; and
- **growth in teacher salaries** – in both fiscal 2007 and 2008, over two-thirds of counties gave teachers annual salary increases of at least 4%.

As of January 31, 2009, the pension fund's fiscal year-to-date investment return is -27.3% for fiscal 2009. For this analysis, Legislative Services expects financial markets to begin to rebound toward the end of the fiscal year in response to the federal stimulus and financial bailout initiatives. Therefore, Legislative Services projects a fiscal 2009 investment return of -20%, followed by a 3% return in fiscal 2010, which assumes that financial markets continue a modest recovery. After that, the analysis assumes that the pension fund earns 7.75% annually, which is the assumed rate of return used by the actuary to calculate annual contribution rates.

Estimating the fiscal effect of this bill beginning in fiscal 2011 on both the State and counties is complicated by the fact that the system's actuary does not allocate the cost of teacher pensions to each county. Instead, the State Retirement Agency (SRA) annually estimates the cost of pensions allocated to each county based on salary and membership projections. However, its estimates do not total the full cost of the TRS/TPS contribution calculated by the actuary. The actuary calculates a fiscal 2010 contribution of $832.6 million, of which an estimated $19.6 million is for members at State higher education institutions, leaving $813.0 million for the counties. However, SRA's county-by-county projections total only $800.8 million. The agency believes the discrepancy is due to the fact that its calculations are rough and do not account for factors such as employee turnover that are included in actuarial calculations.

Although SRA advises that it plans to use its own projections to bill counties for the cost of teacher pensions, Legislative Services believes that such calculations should be performed by the system's actuary. It is more likely that, should this bill be enacted, the system's actuary will allocate the full cost of local pensions to each of the counties as part of its annual valuation of the system. Therefore, for the purposes of this analysis, Legislative Services has adjusted on a prorated basis the agency's estimates for each county so that they are equal to the actuary's total of $813.0 million.

Based on these assumptions and adjustments, and subject to asset smoothing and the corridor method, **Exhibit 2** shows the total employer contributions for the combined teachers' plans projected by the General Assembly's consulting actuary for fiscal 2011 through 2014. The projections assume 3.5% annual increases in both payroll and the normal cost, and 6% annual increases in benefit payments reflecting a combination of payroll increases and more retirements. Almost 2.4% of total contributions is attributed to members employed by State institutions. Under this bill, employer contributions for these members continue to be paid entirely by the State. Therefore, it is assumed that 2.4% of projected annual employer contributions are not shared with counties.

Exhibit 2
Projected TRS/TPS Employer Contributions
($ in Millions)

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
Rate	13.15%	14.27%	15.45%	16.51%	17.84%
Total Contribution	$832.6	$935.2	$1,047.9	$1,159.0	$1,296.2
Total Contribution for Local Members	$813.0	$913.2	$1,023.2	$1,131.7	$1,265.7
State Savings		**$100.2**	**$210.2**	**$318.7**	**$452.7**

Source: Mercer Human Resources Consulting, State Retirement Agency, Department of Legislative Services

Based on these calculations, State general fund expenditures for employer pension contributions decrease by $100.2 million in fiscal 2011, representing the difference between total employer contributions of $813.0 million in fiscal 2010 paid by the State for local TRS/TPS members and projected payments of $913.2 million in fiscal 2011 to be paid by the counties. If the pension fund's investment losses at the end of fiscal 2009 are greater than the projected 20% loss, the savings to the State could be higher. Based on the trends shown in Exhibit 2, Legislative Services projects that State and local parity in employer contributions for TRS/TPS is achieved most likely in fiscal 2017.

Local Fiscal Effect: **Exhibit 3** provides the distribution of the local share of TRS/TPS employer contributions to each county, based on the assumptions and adjustments described above.

Exhibit 3
Distribution of Local Share of TRS/TPS Employer Contributions
($ in Millions)

	FY 2011	**FY 2012**	**FY 2013**	**FY 2014**
Allegany	$1.18	$2.48	$3.76	$5.34
Anne Arundel	8.37	17.56	26.62	37.82
Baltimore City	9.45	19.83	30.06	42.70
Baltimore	11.57	24.27	36.79	52.26
Calvert	1.97	4.13	6.26	8.89
Caroline	0.60	1.25	1.89	2.69
Carroll	3.09	6.48	9.82	13.95
Cecil	1.75	3.67	5.57	7.90
Charles	2.84	5.96	9.03	12.83
Dorchester	0.52	1.09	1.66	2.35
Frederick	4.34	9.10	13.80	19.60
Garrett	0.53	1.11	1.68	2.39
Harford	4.27	8.96	13.58	19.29
Howard	6.81	14.29	21.67	30.78
Kent	0.28	0.59	0.89	1.27
Montgomery	19.68	41.29	62.59	88.90
Prince George's	14.91	31.29	47.44	67.38
Queen Anne's	0.76	1.60	2.43	3.45
St. Mary's	1.70	3.56	5.39	7.66
Somerset	0.36	0.75	1.14	1.62
Talbot	0.44	0.93	1.42	2.01
Washington	2.23	4.67	7.08	10.05
Wicomico	1.62	3.40	5.15	7.32
Worcester	0.94	1.97	2.99	4.24
County Total	**$100.19**	**$210.23**	**$318.72**	**$452.69**

Source: Mercer Human Resources Consulting, State Retirement Agency, Department of Legislative Services

Additional Information

Prior Introductions: None.

Cross File: HB 525 (Delegate Schuh) - Appropriations.

Information Source(s): Baltimore, Garrett, and Montgomery counties; Baltimore City; Baltimore City Community College; Maryland State Department of Education; Maryland Higher Education Commission; Morgan State University; State Retirement Agency; University System of Maryland; Mercer Human Resources Consulting; Department of Legislative Services

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Analysis by: Michael C. Rubenstein

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