Department of Legislative Services

Maryland General Assembly
2010 Session

FISCAL AND POLICY NOTE
Revised

House Bill 775 (Delegate Griffith, *et al.*)
Appropriations Budget and Taxation

State Retirement and Pension System - Retirees and Beneficiaries of Retirees - Annual Retirement Allowance Adjustments

This emergency bill specifies that, if the calculation of the 2010 cost-of-living adjustment (COLA) for retirees and beneficiaries of designated systems of the State Retirement and Pension System (SRPS) results in a negative adjustment, retirement allowances are not to be adjusted for fiscal 2011. The bill also requires, if fiscal 2011 allowances are not adjusted because of a negative COLA calculation, that fiscal 2012 allowances be reduced by the difference between the fiscal 2010 allowances and the allowances that would have been paid in fiscal 2011 if they had been adjusted. The bill also includes a related study and reporting requirement for the SRPS Board of Trustees.

The bill terminates December 31, 2014, except for the bill's reporting requirement, which terminates December 31, 2010.

Fiscal Summary

State Effect: State pension liabilities increase by approximately $7.6 million. Amortizing those liabilities over 25 years results in State pension contributions increasing by $507,000 in FY 2012 and increasing annually according to actuarial assumptions. There may be an actuarial gain the following year that offsets some or all of the annual costs in FY 2013 and thereafter. Costs for teachers are generally paid entirely by general funds, while costs for State employees are assumed to be allocated 60% general funds, 20% special funds, and 20% federal funds. No effect on revenues.

(in dollars)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
Revenues	$0	$0	$0	$0	$0
GF Expenditure	0	425,900	441,000	456,100	472,100
SF Expenditure	0	40,600	42,000	43,400	45,000
FF Expenditure	0	40,600	42,000	43,400	45,000
Net Effect	$0	($507,000)	($525,000)	($543,000)	($562,000)

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

Local Effect: Local pension liabilities for participating governmental units (PGUs) increase by approximately $506,000. Amortizing those liabilities over 25 years results in PGU employer contributions increasing by $34,000 in FY 2012 and increasing annually according to actuarial assumptions. Those costs are shared among approximately 120 PGUs.

Small Business Effect: None.

Analysis

Bill Summary: The bill applies to COLA calculations in fiscal 2011 and 2012 for former members, retirees, and surviving beneficiaries of the following SRPS plans:

- Employees' and Teachers' Pension Systems (EPS/TPS) who receive either a simple or compounded COLA capped at 3%;
- Teachers' or Employees' Retirement System (TRS/ERS) who receive either a compounded COLA capped at 5% or a bifurcated COLA;
- Law Enforcement Officers' Pension System (LEOPS);
- State Police Retirement System (SPRS) for annual COLAs applied to benefit adjustments provided to retirees and beneficiaries beginning in 1999; and
- TRS, ERS, SPRS, and Correctional Officers Retirement System (CORS) who receive uncapped COLAs.

The SRPS Board of Trustees must study (1) the effects of a decline in the Consumer Price Index (CPI) on retiree allowance adjustments in other public pension plans; and (2) actions taken by other public pension plans in response to negative COLA calculations. The board must report its findings, and recommendations to avoid reductions in retirement allowances when the annual CPI declines, to designated committees of the General Assembly by October 1, 2010.

Current Law: Each year, retirement allowances paid to SRPS retirees and beneficiaries are adjusted for inflation. All COLA calculations are based on average annual changes to the CPI for all urban consumers (CPI-U), but the amount and type of COLA varies by system. In general, the various statutory COLA provisions do not prohibit a negative adjustment. COLAs are applied to retiree and beneficiary allowances effective July 1 of each fiscal year based on the average CPI-U as of December 31 of the previous fiscal year.

EPS/TPS and LEOPS retirees and beneficiaries receive annual compounded COLAs, subject to a 3% cap. However, EPS/TPS retirees and beneficiaries of the noncontributory (pre-1998) EPS receive simple (noncompounding) COLAs, also subject to a 3% annual cap. Only eight PGUs, most notably Prince George's County government, participate in noncontributory EPS.

SPRS, CORS, and ERS/TRS retirees and beneficiaries subject to Selection A (*i.e.*, contributed 7% of earnable compensation while active) receive unlimited, compounded COLAs.

ERS/TRS retirees and beneficiaries subject to Selection B (*i.e.*, contributed 5% of earnable compensation while active) receive annual compounded COLAs, subject to a 5% cap. ERS/TRS retirees and beneficiaries subject to Selection C (a bifurcated benefit) receive a two-part COLA. For service credit earned under ERS/TRS, the COLA is unlimited. For service credit earned after choosing Selection C, the COLA is subject to a 3% cap.

Chapter 122 of 1999 increased the retirement allowances of SPRS retirees and beneficiaries of retirees who retired before June 30, 1999, by providing annual lump sum payments, as follows:

- $1,200 for retirees who had been retired not more than 5 years;
- $1,500 for retirees who had been retired more than 5 but less than 10 years;
- $1,800 for retirees who had been retired more than 10 but less than 15 years; and
- $2,100 for retirees who had been retired more than 15 years.

Retirees and beneficiaries receive an annual unlimited COLA on the annual lump sum in addition to their existing benefit and COLA.

Retirees and beneficiaries of the Legislative Pension Plan and the Judges' Retirement System do not receive automatic COLAs, and they are not affected by this bill. Their benefits are linked to the salaries of active legislators and judges, respectively. Therefore, their benefits increase whenever salaries for active members are raised.

Background: The CPI-U declined by 0.356% over the previous year as of December 31, 2009. Specifically, the average CPI-U index was 214.5 for 2009, compared with 215.3 for 2008. This is the first decline in CPI-U on an annual basis since 1954. **Exhibit 1** shows the annual percentage changes in the CPI-U since 2000. As the exhibit shows, the CPI-U has exceeded 3% in 4 of the last 10 years, but has not exceeded 5% in any of those years.

The statutory language governing the various COLA calculations generally does not preclude the application of a negative COLA, which would result in a reduction to retirees' and beneficiaries' annual allowances. However, retirees of SPRS, CORS, and ERS/TRS who are subject to the unlimited COLAs cannot receive an allowance in a given year that is less than their initial allowance. Therefore, retirees of those systems who are in their first year of retirement are protected against a negative COLA because the initial allowance they are receiving this year cannot be reduced.

Exhibit 1
Annual Percentage Changes in CPI-U
Calendar 2000-2009

Year	% Annual Change
2000	3.4
2001	2.8
2002	1.6
2003	2.3
2004	2.7
2005	3.4
2006	3.2
2007	2.8
2008	3.8
2009	-0.4

Source: U.S. Bureau of Labor Statistics

Exhibit 2 shows the number of retirees and beneficiaries in each of the State's major employee pension and retirement plans and their average monthly benefit in fiscal 2009.

Exhibit 2
SRPS Retirees and Beneficiaries
June 30, 2009

Plan	Retirees and Beneficiaries	Average Monthly Benefit
TRS	30,598	$2,600
TPS	25,158	$1,457
ERS (includes CORS)	23,778	$1,530
EPS	32,832	$905
SPRS	2,226	$3,525
LEOPS	1,067	$2,551

Source: State Retirement and Pension System

State Fiscal Effect: The Department of Legislative Services (DLS) assumes that SRPS would, in the absence of this bill, reduce most retirees' and beneficiaries' fiscal 2011 retirement allowances by 0.356% from their fiscal 2010 levels due to a negative COLA calculation for all affected SRPS plans. That results in a one-time overpayment of $7.6 million (compared with current law) to all SRPS retirees and beneficiaries in fiscal 2011. Although the overpayment is recouped the following year by reducing fiscal 2012 benefits by the equivalent amount, the full overpayment in fiscal 2011 is recognized as an actuarial loss in the June 30, 2010 actuarial valuation, and amortized over 25 years. As a result, State pension contributions increase by an estimated $507,000 in fiscal 2012 and increase each year thereafter according to actuarial assumptions. There may be an actuarial gain in the following year (June 30, 2011) that may offset some or all of the out-year costs. State contributions for TRS/TPS members are paid entirely with general funds; contributions for State employees are assumed to be allocated 60% general funds, 20% special funds, and 20% federal funds. Overall, 84% of State pension costs are paid by general funds.

Local Fiscal Effect: Local pension liabilities increase by approximately $506,000; amortizing those liabilities over 25 years yields a first-year cost of $34,000 in fiscal 2012. That cost is presumed to grow annually according to actuarial assumptions and is shared by approximately 120 PGUs. An actuarial gain may be recognized in the following year that offsets some or all of the out-year costs.

Additional Information

Prior Introductions: None.

Cross File: SB 317 (Senator McFadden, *et al.*) - Budget and Taxation.

Information Source(s): Mercer Human Resources, U.S. Bureau of Labor Statistics, Department of Legislative Services

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ncs/rhh	Revised - Correction - March 7, 2010
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