SB 498

Department of Legislative Services

Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE

Senate Bill 498 (Senator Jones-Rodwell)(Chair, Joint Committee on Pensions)

Budget and Taxation Appropriations

State Retirement and Pension System - Contribution Rates and Reinvestment of Savings - Technical Clarifications

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This bill makes technical and clarifying changes to the funding provisions for the State Retirement and Pension System (SRPS). The changes clarify the process for calculating the annual corridor funding contribution to conform to legislative intent and specify that the Governor must include exactly $300.0 million in annual additional contributions above the actuarial rate certified by the board of trustees in the budget bill each year.

The bill takes effect July 1, 2012.

Fiscal Summary

State Effect: None. The bill is technical and clarifying in nature.

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law:

Corridor Funding

The Teachers' Combined Systems and the Employees' Combined Systems of SRPS 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 remained actuarially funded between 90% and 110%. As the plans fell out of the corridor, the employer contribution increased by an amount equal to one-fifth (20%) of the difference between the prior year's rate and the "true" rate required to fully fund the system. The calculation of the corridor funding method is adjusted to reflect legislative changes that result in changes in normal cost and accrued liabilities. The employees' plans fell out of the corridor in fiscal 2005, and the teachers' plans followed in fiscal 2006.

Additional State Contribution

Chapter 397 of 2011 (the Budget Reconciliation and Financing Act) restructured benefits for current and future members of SRPS, generating substantial savings in annual State contributions to SRPS. Major components of the benefit changes included:

- increasing member contributions for most current and future members of SRPS;
- lowering benefit accrual rates for teachers and State employees hired after June 30, 2011, and requiring them to work longer before vesting or becoming eligible for retirement; and
- making the size of retiree cost-of-living allowances for service credit earned after June 30, 2011, contingent on the performance of the system's investment portfolio.

Chapter 397 requires the Governor to include in the budget bill an additional contribution to the pension trust fund, above the required actuarial contribution, that represents a portion of the savings generated by the benefit changes. The purpose of the reinvested savings is to help the State achieve the statutory objective of reaching an 80% actuarial funding level by fiscal 2023. In fiscal 2011 and 2012, the amount of the reinvestment was set at $120.0 million. Beginning in fiscal 2013, the board must calculate the difference between what the State contribution would have been absent the reforms and the actual contribution; the Governor is required to include *up to* $300.0 million of the amount of the difference in the budget, with any excess savings accruing to the State.

Background:

Corridor Funding

When the corridor method was enacted, it was the intent of the legislature that the actuarial effects of any changes to the benefits provided to members that were enacted through legislation not be included in the corridor calculation. Instead, the legislature wanted the funding effects of those changes to be fully recognized in the year they were enacted. When benefits were enhanced for teachers and State employees in 2006 (Chapter 110), the full cost of the enhancement was recognized that year, consistent with legislative intent. However, following the enactment of Chapter 397 of 2011, the State Retirement Agency identified language in the statute that was ambiguous regarding how the funding effects of the benefit changes that were made should be treated under the corridor method. This bill clarifies that the effects of those changes are not subject to the corridor, but instead they should be fully recognized in the year they are enacted. This is consistent with legislative intent and also with previous practice in 2006.

Additional State Contribution

Following the enactment of Chapter 397, the system's actuary advised that from an actuarial perspective, it is increasingly difficult to accurately evaluate a former plan as time passes under the reform plan. Therefore, the statutory requirement to compare contribution rates with and without the reforms could not be implemented. Actuarial projections conducted both by the system's actuary and the General Assembly's consulting actuary indicate that total savings in fiscal 2013 and each year after will exceed the $300.0 million cap instituted by Chapter 397. Therefore, the bill establishes $300.0 million as the required additional contribution by the Governor and repeals the requirement that the board conduct the calculations with and without the reforms.

Additional Information

Prior Introductions: None.

Cross File: HB 807 (Delegate Griffith)(Chair, Joint Committee on Pensions) - Appropriations.

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

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