**SB 665**

# Department of Legislative Services

Maryland General Assembly
2014 Session

## FISCAL AND POLICY NOTE
**Revised**

Senate Bill 665 (Senator Edwards, *et al.*)
Budget and Taxation Appropriations

**Correctional Officers' Retirement System - Membership**

This bill adds correctional officers who begin serving as security chiefs, facility administrators, assistant wardens, or wardens on or after the bill's effective date as members of the Correctional Officers' Retirement System (CORS) as a condition of their employment. It also gives correctional officers who are serving in those positions on June 30, 2014, six months to transfer their service credit from the Employees' Pension System (EPS) to CORS if they continue serving in those positions on the bill's effective date. Transfers of service credit under the bill must be done in accordance with Title 37 of the State Personnel and Pensions Article. The executive director of the State Retirement Agency (SRA) may waive the one-year statutory time limit on transfers of service credit.

The bill takes effect July 1, 2014; the provisions relating to current EPS members terminate December 31, 2014.

## Fiscal Summary

**State Effect:** State pension contributions increase by up to $401,200 in FY 2017. To the extent that not all eligible members of EPS elect to transfer service credit to CORS, total costs are less. Out-year costs increase according to actuarial assumptions and are assumed to be allocated 60% general funds, 20% special funds, and 20% federal funds. No effect on revenues.

| (in dollars) | FY 2015 | FY 2016 | FY 2017 | FY 2018 | FY 2019 |
|---|---|---|---|---|---|
| Revenues | $0 | $0 | $0 | $0 | $0 |
| GF Expenditure | 0 | 0 | 240,700 | 277,700 | 316,200 |
| SF Expenditure | 0 | 0 | 80,200 | 92,600 | 105,400 |
| FF Expenditure | 0 | 0 | 80,200 | 92,600 | 105,400 |
| Net Effect | $0 | $0 | ($401,200) | ($462,800) | ($527,100) |

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

**Local Effect:** None.

**Small Business Effect:** None.

## Analysis

**Current Law/Background:** Membership in CORS is a condition of employment for individuals who are:

- correctional officers in the first six job classifications;
- security attendants at the Clifton T. Perkins Hospital Center;
- correctional dietary, maintenance, and supply officers; and
- specified employees of Maryland Correctional Enterprises.

CORS members are eligible for a normal service retirement after 20 years, as long as their last five years are in CORS-eligible positions. They receive a retirement allowance equal to one fifty-fifth (1.818%) of their average final compensation for each year of service.

CORS members who are promoted out of the first six classifications (for instance, into a supervisory or managerial position like those specified in the bill) are no longer eligible for CORS and become members of EPS as a condition of employment. There are several key differences in the benefit structure between the two plans. EPS members pay a higher employee contribution than CORS members (7% vs. 5%). CORS members are eligible for a normal service retirement after 20 years or at age 55, whereas EPS members hired before July 1, 2011, are eligible for a normal service retirement after 30 years or at age 62 (those hired on or after that date are eligible at age 65 with 10 years of service or they must have a combination of age and service adding to 90). Individuals who join EPS after June 30, 2011, receive a 1.5% benefit multiplier, compared to the 1.818% multiplier for CORS. Some correctional officers have indicated that the loss of CORS membership, and its more generous benefits, can have a deterrent effect on correctional officers accepting promotions to supervisory positions.

Title 37 of the State Personnel and Pensions Article governs the conditions under which members of one State or local pension system can transfer service credit to another State or local pension system. In general, transfers of service credit must occur within one year of the change in employment that prompted a change in membership. However, the SRA executive director may waive the one-year requirement under specified circumstances. In most cases, an individual who transfers service credit receives the same amount of service credit in the new system as was earned in the old system.

The conditions governing transfers of credit vary depending on whether either of the two systems involved in the transfer is noncontributory. For this bill, both EPS and CORS are contributory. However, prior to 1998, EPS was noncontributory. From 1998 to 2006, the EPS member contribution rate was 2%, then it was phased up to 5% in 2008 before being raised to 7% in 2011. By contrast, CORS has always been a contributory system with a 5% member contribution. As explained below, any EPS members eligible to transfer to CORS under this bill who joined EPS prior to July 1, 2008, may have to make additional contributions to transfer their service credit to CORS.

Transfers between two contributory systems like EPS and CORS require the individual to deposit the sum of the following amounts in the annuity fund of the new (CORS) system:

- the total accumulated contributions made to the individual's credit in the old system;
- the difference, if any, between the member contributions made in the old system and the member contributions that would have been made in the new system, including interest; and
- the accumulated contributions that would have been deducted during the period that the individual was a member of a noncontributory State system, including interest.

In the event that these payments are not made in full, at the time of retirement the member's allowance is reduced by the actuarial equivalent of the unpaid amounts.

Thus, an individual transferring to CORS who joined EPS on or after July 1, 2008, and paid a 5% contribution rate does not have to make any additional payments because the contribution rates were identical through fiscal 2011. An individual who joined between 1998 and 2008 will have to pay the difference between the lower EPS rate in effect at the time and the CORS rate, with interest. Finally, an individual who joined EPS before 1998 will have to make the full 5% contribution that would have been required had he or she been a member of CORS at the time, including interest.

In the case of contributory plan to contributory plan transfers, Title 37 is silent regarding the disposition of member contributions made to the old plan that are in excess of the contributions necessary for the new plan. SRA advises that it has been its practice to set aside any excess contribution toward a voluntary annuity for the individual that is available upon retirement. Thus, individuals transferring to CORS from EPS who have paid 7% to EPS since July 1, 2011, would have the 2% excess contribution made during the intervening years set aside for a voluntary annuity. Internal Revenue Code provisions do not allow for that excess amount to be refunded to an individual who remains an active member.

**State Fiscal Effect:** Based on a review of its membership data, SRA advises that 204 current members of EPS were previously members of CORS. However, the Department of Legislative Services advises that an individual does not have to have first been promoted out of CORS into EPS to meet the conditions specified by the bill, although most will have done so. Moreover, the Department of Public Safety and Correctional Services advises that only 70 individuals are in the affected job categories. Although SRA provided data on the age and years of service for each of the 204 EPS members it identified as having prior service credit in CORS, its database does not include job classifications. Thus, the General Assembly's consulting actuary cannot identify which of the 204 individuals are the 70 individuals who are currently wardens, associate wardens, security chiefs, or facility administrators. For this analysis, the actuary calculated the cost of transferring service credit for all 204 individuals from EPS to CORS; the actuary advises that taking a *pro rata* amount of the total cost of transferring that service credit yields an approximate total cost for the 70 individuals.

An earlier analysis by SRA conducted at the request of the Joint Committee on Pensions revealed that, on average, seven individuals are promoted out of CORS into EPS each year. This finding was based on data from 1980 to the present, and the annual number varies tremendously, from a low of zero to a high of 18. For the purpose of this analysis, it is assumed that, absent the bill, seven additional members are promoted out of CORS and into EPS each year. Under the bill, they instead remain in CORS. It is assumed that the demographics of these seven individuals represent the average employee demographics for CORS.

Any transfers from EPS to CORS under the bill occur in fiscal 2015 after the July 1, 2014 effective date. Likewise, beginning in fiscal 2015, each year approximately seven individuals remain in CORS instead of being promoted to EPS. Therefore, the transfers to and individuals maintained in CORS are first recognized in the June 30, 2015 actuarial valuation, which determines State pension contributions for fiscal 2017. Thus, any fiscal effect is delayed until fiscal 2017. As a result of amortizing the increase in pension liabilities over the remaining years of the closed 25-year amortization period and adding in the full normal cost increase advised by the General Assembly's consulting actuary, State pension contributions increase by up to $401,220 in fiscal 2017 for 70 individuals to transfer to CORS and 7 to stay in CORS each year. To the extent that some individuals find the cost of paying for the transfer (by virtue of having to pay the higher CORS member contribution plus interest for some years) too high, the actual number of transfers may be less, thereby lowering the cost. Costs increase in the out-years according to actuarial assumptions and, because CORS is a subsystem of the Employees' Combined Systems, are assumed to be allocated 60% general funds, 20% special funds, and 20% federal funds.

## Additional Information

**Prior Introductions:** None.

**Cross File:** HB 708 (Delegate Serafini, *et al.*) - Appropriations.

**Information Source(s):** Caroline County, Calvert County, Baltimore City, Howard County, Cheiron, Maryland Association of Counties, Montgomery County, Maryland State Retirement Agency, Department of Public Safety and Correctional Services, Prince George's County, Department of Legislative Services

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