STATE RETIREMENT AGENCY
120 East Baltimore Street
Baltimore, MD 21202-6700

MARYLAND
STATE RETIREMENT
and PENSION SYSTEM

410-625-5555 • 1-800-492-5909
TTY Users: call via Maryland Relay
sra.maryland.gov

Testimony for House Bill 115
Teachers' Pension System - Option Election
House Appropriations Committee
January 28, 2020
1:00 P.M.

Anne Gawthrop
Director of Legislative Affairs
State Retirement Agency

The Board of Trustees for the State Retirement and Pension System (System) wishes to express its opposition to House Bill 115, Teachers' Pension System – Option Election. House Bill 115 applies to an individual who: (1) was a member of the Teachers' Pension System (TPS); (2) was employed as a teacher with the Prince George's County public school system on or after January 1, 1988: (3) retired from the TPS on or after June 30, 2017; and (4) at the time of retirement, elected to receive Option 1. An individual described under this bill may elect to change his or her method of distribution from Option 1 to the Basic Allowance or one of the other five available options that provide various survivorship benefits.

We are aware of 74 TPS retirees that currently meet the criteria specified in House Bill 115. Under the provisions of this legislation, each of these individuals would be eligible to alter their initial election to either increase their monthly benefit or provide a more generous survivorship benefit. Current law provides that a retiree may not change his or her benefit election after receiving the first allowance payment after retirement.

Each of the several systems, except the Legislative Pension Plan, provide members with seven different methods of benefit distribution. These seven include the following:

- **Basic Allowance:** For retirees of the Employees', Teachers, and Correctional Officers' Retirement or Pension Systems, a single life annuity based on the retiree's years of service, average final compensation, and benefit multiplier. For retirees of the State Police, Law Enforcement Officers', and Judges' Retirement or Pension Systems, a dual life annuity based on the retiree's years of service, average final compensation, and benefit multiplier, providing a guaranteed survivorship benefit to the retiree's spouse or children.
- **Option 1:** Lump-sum refund payable to the retiree's designated beneficiary equal to the excess of the present value of the reduced basic allowance at the date of retirement minus the total amount of payments made to the retiree's date of death, excluding any cost of living adjustments.
- **Option 2:** 100% joint and survivor annuity, which pays the retiree's surviving designated beneficiary 100% of the retiree's reduced basic allowance for the life of the designated beneficiary.

- **Option 3:** 50% joint and survivor annuity, which pays the retiree's surviving designated beneficiary 50% of the retiree's reduced basic allowance for the life of the designated beneficiary.
- **Option 4:** Lump-sum refund payable to the retiree's designated beneficiary equal to the value of accumulated member contributions minus the total portion of monthly payments attributed to member contributions made to the retiree's date of death, excluding any cost of living adjustments.
- **Option 5:** 100% joint and survivor annuity, which pays the retiree's surviving designated beneficiary 100% of the retiree's reduced basic allowance for the life of the designated beneficiary or returns to the retiree's unreduced basic allowance if the beneficiary predeceases the retiree.
- **Option 6:** 50% joint and survivor annuity, which pays the retiree's surviving designated beneficiary 50% of the retiree's reduced basic allowance for the life of the designated beneficiary or returns to the retiree's unreduced basic allowance if the beneficiary predeceases the retiree.

Once a member is within a year of becoming eligible to retire, a member may request the State Retirement Agency (Agency) to prepare an estimate of benefits for each of these methods of distribution. To prepare this estimate, the member must provide the Agency with the dates of birth of the member and the individual the member would like to name as the member's designated beneficiary. After receiving this information, the Agency determines what the member's monthly benefit would be for the member's Basic Allowance and each of the optional allowances. Staff for the Agency has reviewed each of the 74 accounts that would be impacted by this legislation and each received at least one estimate of benefits prior to retirement (with many accounts receiving multiple estimates). This indicates that these retirees were aware of the reduced benefit they would receive after retirement by not selecting the Basic Allowance and instead selecting a reduced optional allowance. The Committee should also be aware that after the Agency has received the application for retirement from a member that has selected the Basic Allowance, Option 1, or Option 4, the Agency sends a notice to the retiree reminding them that their selection either will not provide any survivor benefits (the Basic Allowance) or may not provide a survivor allowance if there are no funds remaining at the time of the retiree's death (Options 1 and 4). This again indicates that these retirees were reminded that they elected to receive a reduced optional allowance and the risk that there may not be any survivorship benefit available at their death.

As House Bill 115 is drafted, one of two scenarios will occur. Eligible retirees will either: (1) amend their initial Option 1 election to now elect to receive the Basic Allowance for a greater benefit; or (2) amend their Option 1 election to now elect a joint and survivor election that will provide the retiree with a lesser monthly allowance, but will provide the retiree's beneficiary with a lifetime benefit instead of a on-time lump sum payment. Any retiree who opted for the first scenario would likely jeopardize the System's tax qualified status under the federal tax provisions of the Internal Revenue Code and corresponding Treasury regulations. Treasury regulation § 1.401(a)(9)-6 provides that annuity payments made under a defined benefit plan must be non-increasing, except in limited circumstances including cost of living adjustments and statutory changes to the benefit calculation. Under the provisions of House Bill 115, if a retiree were to change his or her election from Option 1 to the Basic Allowance, this actuarial increase to the retiree's annuity would likely violate this regulation.

The Committee should also note that this is not the first time special legislation has been introduced to allow one retiree to unwind the retiree's current benefit, and instead, provide the retiree with a new and potentially increased benefit. Historically, the Board consistently has opposed this type of special legislation. Incidentally, staff for the Agency was unable to find any similar special legislation from past sessions that the Legislature passed. A concern the Board has raised in its previous opposition testimony against this type of special legislation, and that applies again, today, with regard to House

Bill 115, has to do with the effect that the passage of House Bill 115 may have on the actuarial accrued liability, and as such, the employer contribution to the System.

We recognize that as drafted, House Bill 115 will only apply to a small group of people, and that certainly this one change would not have a meaningful impact on the $860.3 million fiscal 2021 TPS employer contribution. In fact, the System's actuary has estimated that if all 74 retirees opted to change from Option 1 to the Basic Allowance (the greatest benefit the retiree could receive), the actuarial accrued liabilities for the System would increase by approximately $10,000 per retiree, or $740,000. However, once one bill is passed that allows for one individual to change his or her retirement benefit, the door is open for all retirees to do so, and as the Committee is well aware, passing one bill makes it that much easier to pass the next.

The parameters regarding who is impacted by House Bill 115 are very narrow in that the bill is limited to Option 1 retired Prince George's County teachers who began employment on or after a certain date and retired by a certain date. Passage of this bill would undoubtedly result in other retirees of the TPS who selected Option 1 requesting similar legislation; or any retiree, for that matter, in any of the several systems who selected Option 1. As of June 30, 2019, 20,916 retirees elected Option 1. If each of these individuals sought legislation to change their election to the Basic Allowance, this would increase the actuarial accrued liability for the System by approximately $209 million. Moreover, if legislation is enacted to allow certain retirees to change their Option 1 election, the Committee should expect to see legislation from members who elected the 100% or 50% joint and survivor election and whose designated beneficiaries have predeceased them, to now elect the Basic Allowance. Or Option 4 retirees who recognize they have depleted their member contributions, resulting in no survivorship benefit for their designated beneficiaries, now seeking legislation to receive the Basic Allowance. As of June 30, 2019, 94,671 retirees elected an optional allowance. This legislation would set a precedent for each of the 94,671 to seek legislation to change their election.

We appreciate being given the opportunity to raise these issues with the Committee and stand ready to provide any further information or services the Committee might request.