

STATE RETIREMENT AND PENSION SYSTEM of MARYLAND

Getting Started

In 1924, Baltimore City established the Employees' Retirement System, which was the first major public pension system in Maryland. The City System applied to its employees as well as the City's public school teachers.

The City System was based on concepts promulgated by Mr. George B. Buck of New York. Mr. Buck's concepts were that employees could receive a retirement income if they contributed a portion of their earnings during their careers. These "employee" contributions would be matched by the employer. Through a lifetime of training in the life insurance actuarial discipline, Mr. Buck determined that a four to six percent contribution by the employee, matched by the employer, could provide an annuity of 1/70th (1.4%) per year of service. An employee who worked 35 years would be capable of retiring with half pay, assuming interest earnings met assumptions.

First State System – the Teachers' Retirement System

The inclusion of Baltimore City teachers in the City's Retirement System caused county school teachers throughout the State to seek similar benefits. In response, the State enacted legislation (Chapter 344 of the Acts of 1927) that established the Maryland State Teachers' Retirement System (TRS). The TRS began its operation as of August 1, 1927. The original TRS benefit was 1/70th of average final compensation (average of last ten years of earnings) with retirement at age 60. Members who continued to teach were permitted to discontinue contributions at age 60 if they had 35 or more years of service.

The 1/70th benefit provided to teachers, and later offered to employees, was not guaranteed. That is, if the required employee and matching employer contributions, with investment returns, did not provide the funding necessary to pay the 1/70th benefit, the State was not obligated to contribute the additional contributions necessary to fund the benefit. It was not until 1962 that the retirement benefit was guaranteed by the State.

Next One In – the Employees' Retirement System

The State Employees' Retirement System (ERS) was established for State employees as of October 1941 (Chapter 377 of the Acts of 1941) with the same benefits provided to members of the Teachers' Retirement System, except normal retirement age was set at 65. Normal ERS retirement age was lowered to age 60 in 1947. Existing members were given the option of electing to increase their employee contributions *or* of accepting a reduced benefit at retirement.

Municipal corporations (counties, incorporated municipalities, special taxing districts or other political subdivisions) were permitted to enroll their employees in the ERS in 1945

(Chapter 969). The municipality was responsible for the employer costs for placing its employees in the ERS. Today 114 municipalities have elected to participate in the employees' systems. The funding and liabilities for these employers are maintained in a separate pool from the State's funding for its pension obligations.

Recognizing Law Enforcement – State Police Retirement System

The State Police Retirement System (SPRS) was established as of July 1949 (Chapter 349). Membership was limited to uniformed officers of the Maryland State Police. The SPRS benefits were designed to recognize the hazardous nature of law enforcement as well as the need to retain a younger police force. In 1956, the State Police were the only group of State employees that did not elect to be included in the federal Social Security Program. Other than Medicare coverage, the members of the SPRS remain outside of the Social Security Program today.

A Constitutional Decision - Legislative Pension Plan

In 1966, Chapter 281 provided for retirement allowances to be paid to members of the Maryland General Assembly. The Legislative Pension Plan (LPP) was established as a subsystem within the Employee' Retirement System. Through legislation enacted in 1970 (Chapter 576) and ratified by voters as a constitutional amendment, a General Assembly Compensation Commission was formed. In 1971, this Commission redesigned the Legislative Pension Plan.

Today legislators receive 3% of legislative salary for each year of service in the General Assembly up to a maximum benefit of two-thirds of legislative salary. Members must accumulate a minimum of eight years of service to qualify for retirement, which is payable at age 60.

A new Legislative Compensation Commission is formed at the close of the legislative session during the third year of each four year legislative term of office. The Commission reviews the salary and benefits of the General Assembly and may amend those benefits as it believes is appropriate. The Commission then presents its report, with its proposed changes, at the beginning of the last active session of a term. The General Assembly may accept or reject the proposed changes, but it cannot amend or add to the proposed LPP benefits. If accepted by the General Assembly, any amendments to the LPP take effect the following year at the start of the new term.

Governor's Benefit

The Governor's benefit is also a subsystem within the Employees' Retirement System. It was established in 1971. It provides benefits only to former Governors and their surviving spouses. For one term in office, a former Governor receives one-third of the current Governor's salary; for two terms the former Governor receives one-half of the current Governor's salary. Payments begin no earlier than age 55.

Era of Change

After many years of relatively minor changes to the employees' and teachers' benefits, the legislature enacted major changes to these systems in the late 60s and early 70s. The ERS/TRS retirement benefit was increased to 1/60th of average final compensation in 1969. In 1970, the vesting requirement was reduced from 20 years to 15 years. An automatic cost-of-living adjustment was enacted in July 1971. Early retirement with reduced benefits, was offered after 25 years of service. The average final compensation was reduced to the three highest years. In 1973, the second major increase to ERS/TRS retirement benefits took the benefit to 1/55th. Retirees who retired prior to July 1, 1970, received a 9% increase to their benefits. Employee contributions were set at 5% and vesting requirements were reduced to five years.

The Mandel "Withdraw" Myth

Governor Mandel pushed for major benefit changes in 1973 based on unexpected revenue that became available following a second actuarial valuation related to the State's pension contributions for that year. The second valuation determined that the funds required as State pension contributions for the year were overstated by approximately \$40 million. Governor Mandel chose to allot a large portion of these "extra" dollars for ERS/TRS benefit improvements – the 1/55th benefit, the 9% increase to retirees, the 5% employee contribution, and the five year vesting. The remaining money was diverted to unrelated State needs.

Timing is always an important element in any event, and the timing of these benefit increases could not have come at a worse time for the System's funding. While the "extra" dollars funded the increase for the first year, these higher benefits required greater State contributions in subsequent years. The higher benefits, together with the long standing practice of pay-as-you-go funding for many benefits, the impact of the automatic, unlimited and compounded cost-of-living adjustments, the double-digit inflation extant at the time and the restrictive investment program seriously undermined the funding status of the System.

In subsequent years, the pension funding issue became a serious fiscal concern which culminated in the establishment in 1980 of two new systems with substantially reduced benefits - the Employees' and Teachers' Pension Systems. Rumor spread that Governor Mandel took money out of the Pension Trust Fund to pay for unrelated State projects and it was his raid on the System that caused the serious under funding of the ERS and TRS. Even though pension law does not permit anyone, including the Governor, to take dollars out of the Trust Fund and, even though the fact is that no one has ever taken money out of the Pension Trust, the myth persists today among long-term members that former Governor Mandel raided the System in the early 1970s.

Stepping Up to the Bench – Judges’ Retirement System

In 1974, a hodgepodge of State and local retirement provisions for judges was replaced with the State’s Judges’ Retirement System (Chapter 483). Judges of the district court, circuit court, court of special appeals and court of appeals, members of the State Workers’ Compensation Commission and full-time masters in chancery or in juvenile causes, appointed on or before June 30, 1989, participate in the Judges’ Retirement System. This plan provides two-thirds of current judicial salary to a judge who retires on or after age 60 with 16 years of service. The employee contribution is 6% of salary for 16 years.

The 20 Year Plan - Correctional Officers’ Retirement System

The Correctional Officers’ Retirement System (CORS) was established in 1974 (Chapter 697). CORS was fashioned from the general provisions of the Employees’ Retirement System. Members contribute 5% of salary to receive a benefit of 1/55th of final average compensation for each year of service. Recognizing the difficulty of the correctional officers’ duties, the General Assembly provided retirement benefits at 20 years, not 30. Retirement benefits are available as early as age 55 with five years of creditable service.

Originally, CORS offered benefits to only the first six job classifications of correctional officers. The system has since been expanded to include: security attendants at Clifton T. Perkins Hospital Center; correctional dietary, maintenance, supply, and laundry officers; and certain specified employees of Maryland Correctional Enterprises. In 2006 CORS was opened up to local governments who wish to include their detention center officers. If they elect to participate, the local government funds that participation.

Portability for Educators – the Optional Retirement Program

In 1975, the General Assembly enacted Chapter 556, which created an Optional Retirement Program (ORP) for higher education employees – employees of the University System of Maryland, Morgan University, St. Mary’s College, Maryland’s Community Colleges, and the Maryland Higher Education Commission. Eligible employees may elect participation in the ORP, a defined contribution plan, in lieu of membership in a State defined benefit plan.

The State contributes 7.25% of a member’s salary to the ORP; employee contributions are not permitted. The Board of Trustees for the State Retirement and Pension System is responsible for selecting the vendors for the ORP as well as the products those vendors may offer under the ORP. The Teachers Insurance Annuity Association and College Retirement Equities Fund (TIAA-CREF) was the original vendor for the ORP. In 1993 Chapter 428 permitted the Board of Trustees to select up to four additional vendors. While the Board has approved up to four vendors in the past, today there are two approved vendors - TIAA-CREF and Fidelity.

Establishing the Employees' and Teachers' Pension Systems

Tier I

In 1979, the General Assembly enacted major changes to the benefits provided to the employees and teachers of the State and employees of the municipal corporations participating in the System. The General Assembly had engaged in a thorough study of the funding of the Employees' and Teachers' Retirement System over a four year period and concluded that sustaining adequate funding levels for those systems was not feasible.

The ERS and TRS were closed to new members effective December 31, 1979. The new law created the Employees' Pension System (EPS) and the Teachers' Pension System (TPS) effective January 1, 1980. The new law also required full advance funding of the new Employee' and Teachers' Pension Systems as well as the Employees' and Teachers' Retirement Systems. It further provided that unfunded liabilities be paid in full by 2020.

All employee and teacher members hired on or after January 1, 1980 were required to enroll in the Employees' and Teachers' Pension Systems. Members of the Employees' and Teachers' Retirement System retained their benefits, but were given the option of transferring to their corresponding pension system and receiving up to a full refund of prior employee contributions with 4% interest.

The Pension Systems were non-contributory for most members. A 5% employee contribution was required only on annual salary that exceeded the Social Security Wage Base for that calendar year. Service credits were accrued based on the number of hours worked with varying standards for Eligibility Service and Creditable Service.

Eligibility Service – the service required to qualify for most benefits - was based on working a minimum of 700 hours in a fiscal year (now 500 hours). If a member worked the minimum hours required in a fiscal year, the member received a full year of Eligibility Service. Only in the first and last year of membership could Eligibility Service be prorated if the member worked less than the required minimum hours.

Creditable Service – the service used to calculate the value of a benefit and to qualify for military service credit – was based on the normal hours worked versus the number of hours worked by a full-time employee. Members who worked less than full-time received pro-rated Creditable Service for part-time employment.

As an example, if a member worked 50% of normal for twelve months of the fiscal year (assume worked 1,000 hours), the member earns one year of eligibility service for having worked more than the minimum hours required during the fiscal year. Assuming full-time is 2,000 hours, this member earns six months of creditable service – 1000 hours worked divided by 2000 hours full-time = .50 times 12 months = six months creditable service.

As another example, imagine a member who begins work March 1 and works 160 hours per month. At the end of that fiscal year, the member will have worked 640 hours. The member earns one year of eligibility service for having worked more than the required minimum hours during the fiscal year. The member also earns four months of creditable service – 640 hours worked divided by 640 hours full-time = 1.00 times four months worked = four months creditable service.

Eligibility for full service retirement in the pension systems remained at 30 years of service, but the retirement age was increased to age 62 (early social security retirement age) and required a minimum of five years of Eligibility Service to retire [age 63-four years; age 64-three years; age 65 or older-two years].

The retirement benefit was set at .008 of average final compensation (AFC) for AFC up to the annual Social Security Integration Level (SSIL) and .015 of any portion of the AFC that exceeded the Integration Level, times years and months of Creditable Service. AFC was redefined as the average of the three highest consecutive years of annual compensation. The Social Security Integration level is the average yearly amount of earnings for which old age and survivor's benefits would be provided under Title II of the federal Social Security Act for an employee 65 years old. The benefit formula is:

- .008 times AFC up to the SSIL times years and months of creditable service, plus
- .015 times AFC in excess of the SSIL times years and month of creditable service.

Early service retirement was provided at age 55 with a minimum of 15 years of Eligibility Service. The early benefit used the service retirement formula and was reduced by .005 for each month retirement preceded age 62 (maximum 42% reduction).

The unlimited compounding cost-of-living adjustment provided under the Employees' and Teachers' Retirement Systems beginning in 1971, which was considered a major reason for the significant increases to employer contribution costs by the late 1970s, was limited to 3% of the initial pension benefit.

Picking Your Poison

The significant changes enacted in 1979 did not fully resolve the funding issues of the past. The unlimited, compounded COLAs of the retirement systems continued to be a concern, while employer contribution costs were increased to comply with the new requirement of full actuarial funding of the current year's cost plus payments towards payments of the unfunded liabilities. These continuing concerns led the General Assembly to enact legislation in 1984 (Chapter 7) that impacted the members of the ERS and TRS. Members of the Retirement System were required to make an election to be effective July 1, 1984, to determine whether to keep their benefits intact, or to elect lesser benefits.

Three selections were provided.

- Plan A - permitted members to increase their contribution by 2% (to 7% for most members) and retain all retirement system benefits, including the unlimited compounded COLA.
- Plan B – permitted members to maintain their current employee contribution level (generally 5%) and keep all retirement system benefits except COLAs, which were capped at 5%; and,
- Plan C – established a two-part benefit. The benefit for service accrued prior to electing Plan C was calculated under the retirement system formula and service accrued after the election was calculated under the pension system formula.

An additional incentive – a higher interest rate - was added to encourage retirement system members to elect to transfer all accrued credit to a pension system. At transfer, the member received up to a full refund of employee contributions with interest based on a rolling five year average of System investment returns. This enhanced interest rate was applied to employee contributions from the date of initial membership through date of refund, replacing the normal 4% interest return earned during membership in a retirement system.

The enhanced interest rate for transferring reached as high as 15.9% in the mid 1990s. These high rates produced large refund amounts and influenced many retirement system members to transfer to a pension system and roll their refunds into other tax deferred investments. In 2006, with lower interest rates and fewer members electing to transfer, the General Assembly eliminated the option of transferring to a pension system, as well as permitting retirement system members to step down in their plan selections (Plan A dropping to Plan B or Plan C, or Plan B dropping to Plan C).

In response to the 1984 legislation that mandated retirement system members make a choice to retain their existing pension benefits, the Maryland State Teachers Association, and other employee groups, filed suit in federal court alleging that the legislation violated constitutional contractual rights. The unions referred to the new law as giving members the right to “pick your own poison”. The case was dismissed by the federal District Court through a declaratory ruling and the decision was upheld by the United States Fourth District Court of Appeals.

Tier II – Contributory Pension Systems

While the 1979 and 1984 legislation greatly improved the financial and actuarial status of the System, there was growing concern, particularly within the Board of Trustees, that the benefits of the Employees’ and Teachers’ Pension Systems were inadequate to meet the needs of many public employees. Although most members did not contribute to the pension system, few elected to or were capable of redirecting a portion of their income into private saving. Furthermore, changes to social security drove up the annual Social Security Wage Bases – the amount of annual earnings subject to the social security tax – producing a higher SSIL, which placed more pension system members’ AFC below the

Integration Level. This meant that a greater portion of the membership were to receive 24% of AFC for 30 years of membership. Original projections had assumed the average member would receive 30 to 33% of AFC as an annual benefit.

Through the joint efforts of the retirement System's Board of Trustees, the Joint Committee on Pensions and the leadership of the Maryland General Assembly, benefits were greatly enhanced by the establishment of a second tier within the Pension Systems, the Contributory Pension System (Chapter 530 of the Acts of 1998).

The implied integration with Social Security, as provided under the original Pension Systems, now known as the Non-Contributory Pension Systems, was eliminated. The Contributory Pension System returned to a flat benefit multiplier for years of service. Members were to receive 1.2% of AFC for all service credits accrued on or before June 30, 1998, and 1.4% of AFC for all service accrued on and after July 1, 1998. COLAs were increased to 3% compound. Members were required to contribute 2% of salary from July 1, 1998 for the new, higher benefit. For those who were to work 30 years under the 1.4% multiplier, the benefit returned to a more reasonable 42% of AFC.

Adding Municipalities

The new law applied to all State employees and teacher members except for those who transferred from a retirement system to a pension system on or after April 1, 1998. Municipal corporations were initially excluded from this legislation at their request. However, after a year of discussion, including projections of additional costs, Chapter 176 of the Acts of 1999 was enacted which permitted participating municipalities to make an irrevocable decision to elect membership in the Contributory Pension System retroactive to July 1, 1998. Most participating employers agreed to participate in the Contributory Pension System and pay the higher costs. A handful of employers, including Prince Georges' County Government, elected to remain in the Non-Contributory Pension System. Employers that began participation in the System on or after July 1, 1998 had to participate in the Contributory Pension System.

Those employers that remain in the Non-Contributory Pension System as of 2008 are:

- Anne Arundel Economic Opportunity Council
- Town of North Beach
- Prince George's County Government
- Prince George's County Crossing guards
- City of Crisfield
- Crisfield Housing Authority

Tier III - Alternate Contributory Pension Selection

The last major enhancement to the Employees' and Teachers' Pension Systems to date, occurred as of July 1, 2006 when the General Assembly established the Alternate Contributory Pension Selection, ACPS (Chapter 110). All State employees and teacher members were required to participate in the ACPS. Municipalities were given the option

to pay the additional costs and participate in the ACPS. Those municipalities that elected to remain in the Contributory Pension System are the cities of: Emmitsburg, Frostburg, Middletown, and Taneytown. Frederick County, a withdrawn municipality, obtained special legislation to permit its employees who remain under the pension system to participate in the ACPS with the County funding the additional costs.

Under this new third tier within the pension systems, members continue to receive 1.2% of AFC for service accrued on or before June 30, 1998, except for military service credit which receives the highest benefit multiplier offered at time of retirement. The 1.4% benefit of the Contributory Pension System was replaced by a 1.8% benefit multiplier retroactive to July 1, 1998. The employee contribution was increased to 3% as of July 1, 2006, 4% as of July 1, 2007, and 5% as of July 1, 2008. It will remain at 5%. There was no change to the COLA which remains at 3% compounded.

The Rest of Law Enforcement – Law Enforcement Officers’ Pension System

The Natural Resources Law Enforcement Officers’ Pension System was established as of July 2, 1990, specifically for the uniformed law enforcement officers and park rangers of that department who had been promised pension benefits similar to those provided to the Maryland State Police. The new system provided for retirement benefits at age 50 or after 25 years of service and provided death and disability benefit which took the hazardous duties of law enforcement into consideration. Different levels of benefits were established for those officers and park rangers who transferred from the Employees’ Retirement System and the Employees’ Pension System to the DNR plan.

The original pension system benefits were similar to the EPS/TPS benefits, providing 1.0% of AFC up to the SSIL and 1.7% of AFC in excess of the AFC. A special provision provided the 1.7% benefit on all salary up to age 62 after which it was to be lowered to the benefit levels noted above. For those members who transferred from the ERS, the benefit was 2.0% of AFC for up to 30 years of service, and 1.0% of AFC for each year over 30.

Beginning in the mid 1990s, the General Assembly determined that the system should be expanded to all of the State’s law enforcement personnel, except State Police. The system’s name was changed to the Law Enforcement Officers’ Pension System (LEOPS) and membership was expanded to include State law enforcement personnel as well as State fire fighters at BWI Thurgood Marshall Airport and Martin State Airport. In 1998, LEOPS was opened up to local governments for their law enforcement officers, fire fighters and paramedics.

In 2000, LEOPS retirement benefits were enhanced. Members were required to contribute 4% of annual salary. The integrated benefit formula was replaced with a flat benefit multiplier of 2.0% for each year up to a maximum 30 years, or a maximum benefit of 60% of AFC. Members, who continue working after 30 years, pay the 4% contribution, but do not earn additional service credits. For those who transferred from

the ERS, the benefit was increased to 2.3% of AFC for the first 30 years of service and remained at 1.0% of AFC for years over 30.

Gone But Not Forgotten - Local Fire & Police System

Effective July 1990, acting on the request of numerous Maryland municipalities, the General Assembly established the Local Fire & Police System to permit local governments to provide a benefit structure that recognized hazardous duty for its law enforcement and public safety employees. The system offered retirement after 25 years of service or upon reaching age 50.

Originally, this system was to closely resemble the DNR system. Several interested municipalities argued, however, that they could not afford the higher proposed costs and, as a result, proposed benefits were scaled down. Death and disability benefits that recognized the hazardous nature of law enforcement were deleted and the integrated retirement formula was set at 1.0% and 1.5%. If the employer did not participate in social security, the retirement benefit was fixed at 1.5% of AFC.

While employers argued that the most important element in the new plan was the 25 year retirement, the proposed benefits proved inadequate. Few municipalities elected to participate and the majority of those that did, transferred their employees' memberships to LEOPS when that system was opened to local governments.

With little interest remaining in this system, the Local Fire and Police System was closed to new employers in 2005. As of July 1, 2008 all participating employers had elected to withdraw and transfer their employees to LEOPS.