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Maryland Pension Reform: Does the Law Allow It?

ROCKVILLE, MD (July 24, 2017) — Maryland lawmakers can legally change future pension benefits for state employees as long as those changes are found to be reasonable, according to a new analysis from the Maryland Public Policy Institute. With Maryland's state employee pension system facing a $20 billion shortfall, the report sheds new light on the legal precedent that will influence the size and scope of pension reform in Maryland. View the full report at mdpolicy.org.

"Nearly 400,000 current and retired Maryland state employees depend on the State Retirement Pension System for a secure retirement," said Christopher B. Summers, president of the Institute. "With the pension system in dire fiscal straits, this report offers clarity on which elements Maryland lawmakers can alter and which elements enjoy strong protections under the law."

According to the report, pension benefits earned by a public employee through services already performed enjoy strong legal protections. Lawmakers have more freedom, however, to alter future employee benefits. The Maryland Court of Special Appeals has held that "reasonable" changes can be made to the rate of future benefit accrual if they help the system satisfy its obligation to pay benefits "without serious detriment to the employee."

Because enhancing the system's actuarial soundness is considered a reasonable change, state and local governments have standing to make future changes that enhance plan funding.

The report is authored by Amy B. Monahan, the Melvin C. Steen Professor of Law at the University of Minnesota. Professor Monahan specializes in federal taxation and employee benefits law. She was awarded the American Law Institute's 2013 Young Scholars Medal for her work on public pensions and health care reform.

"In many states, it is difficult to have productive political debate about public pension reforms because the extent of legal protections for such benefits is often unclear," said Professor Monahan. "Maryland is in an advantageous position because its state law is comparatively clear. Knowing that accrued pension benefits are entitled to strong protection, while prospective changes to such benefits are generally permissible, gives Maryland lawmakers the ability to structure reforms that are within the bounds of existing law."

The primary reason for Maryland's pension funding shortfall is that the fund consistently underperforms its investment target. The fund's stated goal is to return an average of 7.55% per year, but has only averaged 4.85% per year the past 10 years. The returns fell into the bottom 10 percent of the fund's peer group over that same time period, implying an opportunity cost of about $400 million per year or $4 billion overall.

About the Maryland Public Policy Institute: Founded in 2001, the Maryland Public Policy Institute is a nonpartisan public policy research and education organization that focuses on state policy issues. The Institute's mission is to formulate and promote public policies at all levels of government based on principles of free enterprise, limited government, and civil society. Learn more at mdpolicy.org.

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