Economic Impact Statement

Office of Legislative Oversight

Bill 23-22 Personnel and Human Resources – Pension Amount – Group G

SUMMARY

The Office of Legislative Oversight (OLO) anticipates that enacting Bill 23-22 would have a significant negative impact on economic conditions in the County in terms of the Council's priority indicators. By increasing the benefit accrual rate for accumulated sick leave and potentially affecting employee behavior regarding sick leave accumulation and time of retirement, the Bill would increase total annual pension earnings for current and future Montgomery County Fire and Rescue Services (MCFRS) employees who participate in the Employees' Retirement System. Based on the low rates of County residence among retired and active MCFRS employees, a minor share of the total annual pension increase likely would go to residents. Instead, the Bill likely would generate significant capital outflows in the form of government revenue used to fund pension increases for the majority of retired MCFRS employees who would reside outside the County. OLO expects capital outflows to significantly outweigh the local economic benefits of the change in the pension plan. Moreover, capital outflows caused by the policy change would occur indefinitely if low rates of County residence among MCFRS retirees continue. Because there are no indications current residence patterns among MCFRS employees and retirees will drastically change, OLO believes the negative impacts of the Bill would be significant in the long term.

BACKGROUND

The goal of Bill 23-22 is to amend the County Code to implement a provision collectively bargained between the County Executive and the International Association of Fire Fighters (IAFF).[1] If enacted, the Bill would increase the annual pension amount for Group G members who participate in the Montgomery County Employees' Retirement System.[2] Eligible Group G members include personnel within the Montgomery County Fire and Rescue Services (MCFRS), namely full-time and career part-time paid firefighters, fire officers, and rescue service personnel.[3] For retired MCFRS personnel under the Social Security retirement age, the benefit accrual rate for each year of credited service received for accumulated sick leave would increase to 5% of average final earnings from the current level of between 2% and 2.5%. Once members reach Social Security retirement age, the benefit accrual rate would be 3.4375%.[4]

[1] Legislative Request Report.
[2] "Summary Description for Sworn Fire Personnel in Retirement Group G."
[3] Ibid.
[4] Bill 23-22; Wellons to Council, Memorandum; OMB, Fiscal Impact Statement.

INFORMATION SOURCES, METHODOLOGIES, AND ASSUMPTIONS

Per Section 2-81B of the Montgomery County Code, the purpose of this Economic Impact Statement is to assess the impacts of Bill 23-22 on residents and private organizations in terms of the Council's priority economic indicators and whether the Bill would have a net positive or negative impact on overall economic conditions in the County.[5]

In this statement, OLO identifies the pathways through which Bill 23-22 would increase pension payments to current and future MCFRS employees who participate in the Employees' Retirement System. OLO then estimates: (a) how much of the total annual pension increase likely would go to resident and nonresident households; (b) the value-added from increased household expenditure by County-based pension recipients; and (c) the magnitude of the capital outflow in the form of government revenue used to fund pension increases for nonresidents.

Because OLO does not know how County revenues used to fund the pension increases would otherwise be used in the absence of enacting Bill 23-22, OLO limits the scope of the analysis to the economic impacts of increased pension payments vis-à-vis the estimated capital outflow. That is, this analysis does not account for the economic impacts of alternative government spending or tax cuts in the amount of the capital outflow. Thus, OLO's determination on the Bill's overall economic impact is based on whether the value-added is greater or less than the estimated capital outflow.

The analysis here draws on the following sources of information:

- Interviews with County analysts on the Bill's impact on the pension plan;
- OMB's Fiscal Impact Statement for Bill 23-22;
- Data on the residence of active and retired MCFRS employees provided by the Office of Human Resources (OHR); and
- RIMS II multipliers.

VARIABLES

The primary variables that would affect the economic impacts of enacting Bill 23-22 are the following:

- total annual pension payments;
- place of residence;
- total annual sick leave accumulation;
- average time of retirement; and
- total annual overtime.

[5] Montgomery County Code, Sec. 2-81B.

IMPACTS

WORKFORCE ▪ TAXATION POLICY ▪ PROPERTY VALUES ▪ INCOMES ▪ OPERATING COSTS ▪ PRIVATE SECTOR CAPITAL INVESTMENT ▪ ECONOMIC DEVELOPMENT ▪ COMPETITIVENESS

Residents

OLO anticipates that Bill 23-22 would have overall negative impacts on County residents.

Resident MCFRS Employees

The Bill would primarily benefit current and future MCFRS employees. By increasing the benefit accrual rate for accumulated sick leave, MCFRS personnel who participate in the Montgomery County Employees' Retirement System would receive a net increase in total pension earnings during their future retirement.

In its Fiscal Impact Statement, the Office of Management and Budget (OMB) estimated the impact of the change in the benefit accrual rate on total County contributions for accumulated sick leave based on 1,166 active Group G members as of July 1, 2021. As indicated in **Table 1**, the rate change would increase total County contributions by $9,190,045 over the next six fiscal years,[6] with an average annual increase of $1,598,269.[7] The average per employee County contributions would be $7,882 over six years and $1,371 per year on average. Holding all else equal, increases in County contributions for accumulated sick leave would increase household income for future MCFRS retirees.

Table 1. County Contributions from the Increase in Sick Leave Benefit Accrual Rate ($)

	Total County Contributions	Per Employee Contributions
FY23 (9 months)	1,108,408	951
FY24	1,522,213	1,306
FY25	1,567,880	1,345
FY26	1,614,916	1,385
FY27	1,663,364	1,427
FY28	1,713,264	1,469
Six-Year Total	9,190,045	7,882
Annual Average	1,598,269	1,371

The Bill may also affect pension earnings through behavioral changes regarding sick leave accumulation and/or time of retirement which are unaccounted for in OMB's estimates due to their difficulty to estimate.[8] If the change in the benefit accrual rate incentivizes certain MCFRS personnel to accumulate more sick leave than they otherwise would in the absence

[6] OMB estimated the fiscal impact of the Bill for 9 months of FY23. The annual averages reflect 5.75 years, not 6.
[7] OMB, Fiscal Impact Statement.
[8] Ibid.

of the policy change, they would experience a net increase in their monthly pension payments. If the change incentivizes certain MCFRS personnel to retire earlier than they otherwise would absent the benefit change, they would receive monthly pension payments at an earlier age.

Importantly, the Bill's impacts to County residents (as well as businesses) largely would depend on how many affected MCFRS employees *reside within the County*.

Data from the Office of Human Resources (OHR) on the residence of *active* and *retired* County employees indicate that far fewer MCFRS employees who would reside within the County during retirement would benefit from the pension increase than those who would reside outside the County. As shown in **Table 2**, 19% (242) of active MCFRS personnel reside in the County and 81% (1,004) reside elsewhere. (MCFRS personnel are an outlier in this way, as 60% of non-MCFRS employees reside in the County.)

Given the region's comparatively high rates of senior net migration losses due largely to lack of affordability,[9] it is unsurprising that fewer current pension recipients reside locally than active MCFRS employees. In fact, 15% of retired MCFRS employees and beneficiaries (e.g., surviving spouse) who participate in the Employee's Retirement System currently live in the County. See **Table 2**.

Thus, OLO anticipates the pension increases would positively impact a minor segment of County residents.

Table 2. Place of Residence for Active and Retired MCFRS Employees

	Montgomery, MD	Other Jurisdictions
Active MCFRS Employees	242	1,004
	19%	81%
Retired MCFRS Employees and Beneficiaries	76	516
	15%	85%

Data Source: OHR

Capital Outflow

While County-based MCFRS retirees would benefit from Bill 23-22, OLO believes its overall economic impact on residents would be negative because it likely would result in a significant capital outflow in the form of government revenue flowing out of the County to nonresident households.

Table 3 presents estimates of the amount of County contributions that would go towards resident and nonresident pension earnings, based on current residence of retired MCFRS employees and their beneficiaries. As shown in **Table 3**,

[9] See, for example, Ostrowski, "Best and Worst States for Retirement 2022"; and Frey, "How migration of millennials and seniors has shifted."

the average annual pension increase likely would be $239,740 for residents and $1.4 million for nonresidents over the next six fiscal years. The average annual net capital outflow likely would be $1,118,788.

Table 3. County Contributions by Residence

	County Contributions	Residents 15%	Nonresidents 85%	Difference
FY23	1,108,408	166,261	942,147	(775,886)
FY24	1,522,213	228,332	1,293,881	(1,065,549)
FY25	1,567,880	235,182	1,332,698	(1,097,516)
FY26	1,614,916	242,237	1,372,679	(1,130,441)
FY27	1,663,364	249,505	1,413,859	(1,164,355)
FY28	1,713,264	256,990	1,456,274	(1,199,285)
Six-Year Total	9,190,045	1,378,507	7,811,538	(6,433,032)
Annual Average	1,598,269	239,740	1,358,528	(1,118,788)

Even when accounting for the multiplier effect of increasing pension payments to County residents, the change in law would result in a net capital outflow. The multiplier effect captures how changes in economic activity affect other rounds of spending, and how additional spending impacts certain economic indicators. To illustrate, an increase in household income may in turn increase demand for local restaurants, resulting in restaurant owners hiring more workers.

Using the Regional Input-Output Modeling System (RIMS II) "final-demand multipliers" for Montgomery County developed by the U.S. Bureau of Economic Analysis,[10] OLO estimates the $239,740 increase in the average annual pension payments to residents would increase household spending, resulting in an additional $118,336 in value-added, i.e., the total value of income generated from production (equivalent to gross domestic product). However, as shown in **Table 4**, the combined economic impact of the pension gain to residents and value-added does not make up the total difference of the capital outflow.

Table 4. Estimated Net Capital Outflow

	Residents	Nonresidents	Difference
Annual Average	239,740	1,358,528	(1,118,788)
Value-Added	118,336	.	.
Combined	358,076	.	(1,000,452)

In sum, Bill 23-22 would increase pension earnings for certain MCFRS retirees who would reside in the County during retirement. Other residents would benefit from the value-added generated through increased household spending, for example, increased employment and earnings. However, these secondary impacts likely would be marginal on an annual

[10] U.S. Bureau of Economic Analysis, RIMS II.

basis. More importantly, OLO anticipates the capital outflows to nonresident pension recipients to significantly outweigh the benefits to residents. For this reason, the Bill likely would have an overall negative economic impact on residents.

Beyond these impacts, OLO does not expect the Bill to affect other priority indicators of the Council.

Businesses, Non-Profits, Other Private Organizations

OLO anticipates that enacting Bill 23-22 would have mixed, yet overall negative, impacts on private organizations in the County. Higher pension payments to residents likely would increase household spending on goods and services, benefiting certain County-based businesses. However, as indicated in **Table 4**, the value-added generated from greater household spending would not make up the total difference of the net capital outflow. OLO expects this loss of economic activity to result in foregone business income and employment.

Net Impact

In sum, based on the low rates of County residence among currently retired and active MCFRS employees, Bill 23-22 likely would generate significant capital outflows in the form of government revenue used to fund pension increases for the majority of retired MCFRS employees who would reside outside the County. OLO expects capital outflows to significantly outweigh the increase in pension earnings to resident MCFRS retirees and the value-added from increased household spending on an annual basis. Moreover, if rates of County residence among MCFRS retirees continue, capital outflows caused by the change in the pension plan would occur indefinitely. OLO sees no indication current residence patterns among MCFRS employees and retirees will drastically change. Therefore, OLO believes the negative impacts of the Bill would be significant in the long term.

DISCUSSION ITEMS

Not applicable

WORKS CITED

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Ostrowski, Jeff. "The Best and Worst States for Retirement 2022." Bankrate. August 18, 2022.

"Summary Description for Sworn Fire Personnel in Retirement Group G." Montgomery County Employee Retirement Plans. August 2021.

U.S. Bureau of Economic Analysis. *RIMS II: An Essential Tool for Regional Developers and Planners*. December 2013.

CAVEATS

Two caveats to the economic analysis performed here should be noted. First, predicting the economic impacts of legislation is a challenging analytical endeavor due to data limitations, the multitude of causes of economic outcomes, economic shocks, uncertainty, and other factors. Second, the analysis performed here is intended to *inform* the legislative process, not determine whether the Council should enact legislation. Thus, any conclusion made in this statement does not represent OLO's endorsement of, or objection to, the Bill under consideration.

CONTRIBUTIONS

Stephen Roblin (OLO) prepared this report.