

PUBLIC SCHOOL RETIREMENT REVISIONS

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Senate Bill 1227 (H-9)

Sponsor: Sen. Jud Gilbert

House Committee: Oversight and Investigations

Senate Committee: Appropriations

Complete to 4-27-10

A SUMMARY OF SENATE BILL 1227 (H-9) As Passed by the House

The bill would amend the Public School Employees' Retirement Act (MCL 38.1304 et al.) to make the following changes to the Michigan Public School Employees' Retirement System (MPSERS) benefits:

Retirement Incentives for MPSERS Employees

Currently MPSERS employees have to be age 55 and have 30 years of service to be eligible to retire in the Basic plan or may retire with 30 years with no minimum age requirement under the Member Investment Plan (MIP). The bill would allow employees to be eligible if they had a combined age and years of service totaling 80 for employees who retire between June 15 and October 1, 2010. Retirees would have to apply between May 1 and June 1, 2010 and would have until June 25, 2010 to withdraw their application.

In addition, the bill would provide a 1.7% multiplier in the pension formula for an employee who retires between June 15 and July 1, 2010 and would provide a 1.6% multiplier for an employee who retires after July 1 but by October 1, 2010. Currently a member's pension calculation equals their final average compensation (FAC) multiplied by their years of service multiplied by 1.5%. This would increase a retiree's pension allowance by 6.7% at the 1.6% multiplier or by 13.3% at the 1.7% multiplier. The bill would cap the final average compensation to which the additional multiplier was applied at \$114,000.

The bill would allow for a superintendent or chief administrator to request an extension to allow an employee to remain until July 1, 2011. An extension would require approval by the State Superintendent of Public Instruction.

The bill would require that the additional costs to the pension system created by the increased multiplier and the early out be amortized over a 5-year period.

3% Contribution into Irrevocable Trusts for Retiree Health Care

Beginning October 1, 2010, the bill would require that all MPSERS employees contribute 3% of their compensation into a funding account, which under the bill would mean an irrevocable trust which would be established under House Bill 4073, the Public Employee Retirement Health Care Funding Act, and would be established and administered under Section 115 of the Internal Revenue Code. Employees who earn less

than \$18,000 annually would have to contribute 1.5% for FY 10 but would contribute 3.0% in subsequent years.

Funds deposited in the irrevocable trust could be used to pay for retirement health care benefits for retirees and their eligible dependents now or in the future. The bill would also determine and credit regular interest for employee contributions paid into the trust in the same manner as interest amounts for the Member Investment Plan under Section 33.

Public School Academies (PSAs) and Third-Party Contracts

The bill would remove the exemption of PSAs, as defined in the Revised School Code, from MPSERS. In addition the bill would amend the definition of public school employee for the purposes of this act to include persons working in a reporting unit, or employer, who are employed by a third party. This would require that reporting units pay the contribution rate on the wages of all persons working in a reporting unit even if they are employed by a third party, except for in certain limited circumstances. This would not include a PSA employee who receives retirement benefits under the Optional Retirement Act of 1967. The bill would also require that a retiree that worked for a reporting unit would have to reimburse the retirement system for the amount of the MPSERS contribution rate multiplied by their wages and would allow the retirement system to deduct the payment from their pension allowance.

Phased Retirement Option

The bill would also include an option for retirees under which the employee could retire and draw their pension while still working part-time. An employee would have to reduce the number of hours worked by 50% and work no more than 1,040 hours. The option could be renewed annually but could not exceed a total of 3 years. This option would have to be approved by the reporting unit.

Revise Reporting Unit Requirements

Currently each reporting unit, or employer, is required to forward both employer and employee contributions to MPSERS monthly. The bill would change it to a schedule and manner determined by the retirement system.

In addition, the bill currently requires quarterly affidavits certifying aggregate reportable compensation, sources of contributions, and federal wages, and an annual report listing the persons employed with salary, service, and contributions. The bill would instead require a report every pay period, which includes persons employed as well as wages, amounts paid, hours, and contributions required under the act.

The bill would also require a reporting unit to pay a daily late fee not less than \$25 and interest charges not less than 6% if they fail to correct errors prior to discovery by the retirement system or if errors are found to be intentional.

Provide Supplemental Appropriation for the Office of Retirement Services

The bill would provide \$4.5 million for FY 2009-10 for the Office of Retirement Services, which is in the Department of Technology, Management, and Budget, for administering the changes required under the bill. The appropriation would be designated a work project and the funds could be carried forward for use in FY 2010-11.

Tie-Bar

This bill would not take effect unless House Bill 4073, which would create the Public Employee Retirement Health Care Funding Act, is enacted.

FISCAL IMPACT:

Note: The fiscal information in this summary has been revised based on relevant actuarial data provided by the State Budget Office subsequent to House passage of the bill.

The bill could create both substantial costs and savings—all of which would be local and would be experienced by the employers in MPSERS, which include public school districts, intermediate school districts, participating universities, community colleges, public school academies, and certain libraries.

Retirement Incentives

Increasing the pension calculation multiplier from 1.5% to 1.7%, along with allowing employees to leave as long as they have a combined 80 in age and years of service credit could cost between \$3.7 billion at a 50% participation rate and \$7.4 billion at a 100% participation rate. The costs would be distributed over the next 6 years, but would potentially be partially offset by an estimated \$2.1 billion to \$4.3 billion in savings from replacing fewer employees and due to the salary differential for new employees. However, the estimated cost increases due to the multiplier would be diminished to whatever extent employees retire after July 1 and qualify for a 1.6% multiplier rather than 1.7%. The savings to each MPSERS employer would vary depending on the extent to which each employer's staff could be reduced through retirements, while the costs would be shared by all MPSERS employers because they would be distributed statewide through increased employer contribution rates.

These estimates assume that employers would replace 90%; to the extent that there are fewer replacements the savings would increase. To the extent that the bill would allow districts to avoid layoffs, the bill would also create an indeterminate amount of savings by decreasing unemployment costs.

3% Contribution into Irrevocable Trusts for Retiree Health Care

Requiring an employee contribution of 3% for MPSERS employees toward retirement health care would allow for a reduction in the employer contribution. Estimated savings would be between \$270 and \$291 million depending on the number of retirements for FY 2010-11 and could total between \$2.7 billion and \$2.9 billion over ten years. This provision would create savings only if the increased employee contributions are used to reduce the employer contribution rate as opposed to being saved to pay for future retiree health costs.

Public School Academies (PSAs) and Third-Party Contracts

Requiring employers to pay the MPSERS contribution rate on wages paid to persons working in the reporting unit but employed by a third party would have an indeterminate fiscal impact on MPSERS employers. The provision may increase costs for some employers that pay a significant portion of wages in contracted services, but could create savings statewide by increasing the funds paid to the pension system and potentially

lowering retirement contribution rates. Additionally, requiring retirees who work on contract to reimburse the retirement system would increase funds paid to the pension system and could potentially lower retirement contribution rates. However, there are no data available to determine the fiscal impact of these provisions.

Ten-Year Net Savings/Costs

See the attached tables for a ten-year analysis of projected net savings/costs of the bill with participation assumptions of 50%, 75%, and 100%. While the bill would create savings in the first year, this is because of an actuarial lag such that the added costs of the retirement incentives are not borne by the MPSERS employers until years 2-6. During that period, the incentives create a significant annual net cost, which vary significantly depending on the number of eligible employees that participate. Depending on participation, the estimated net savings/costs would range from a savings of \$1.4 billion with 50% participation to a net cost of \$400 million at 100% participation. As the participation rate increases, the increased pension and retiree health care costs begin to outweigh the initial replacement savings as well as the long term savings achieved by the 3% employee contribution for retiree health care.

ORS Appropriation

Finally, the bill would appropriate \$4.5 million for FY 2009-10 for the Office of Retirement Services for implementation costs.

Fiscal Analyst: Bethany Wicksall

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.

**Estimated Fiscal Impact of SB 1227 (H-9)
@ 100% Participation
(in millions)**

	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	Cumulative 10 Year Total
Increase Multiplier to 1.7% w/ 80out	\$0.0	(\$1,001.0)	(\$1,001.0)	(\$1,001.0)	(\$1,001.0)	(\$1,001.0)	\$0.0	\$0.0	\$0.0	\$0.0	(\$5,005.0)
Increased Retiree Health Costs	(\$590.0)	(\$590.0)	(\$590.0)	(\$590.0)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	(\$2,360.0)
Years of Service 30yr Cap	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
3% Employee Contribution	\$270.0	\$270.0	\$270.0	\$270.0	\$270.0	\$270.0	\$270.0	\$270.0	\$270.0	\$270.0	\$2,700.0
Eliminate Retiree Dental/Vision	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Hybrid Plan for New Employees	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Replacement Savings at 90%	\$1,422.1	\$1,137.7	\$853.3	\$568.9	\$284.4	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$4,266.4
GROSS SAVINGS	\$1,102.1	(\$183.3)	(\$467.7)	(\$752.1)	(\$446.6)	(\$731.0)	\$270.0	\$270.0	\$270.0	\$270.0	(\$398.6)

**Estimated Fiscal Impact of SB 1227 (H-9)
@ 75% Participation
(in millions)**

	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	Cumulative 10 Year Total
Increase Multiplier to 1.7% w/ 80out	\$0.0	(\$750.8)	(\$750.8)	(\$750.8)	(\$750.8)	(\$750.8)	\$0.0	\$0.0	\$0.0	\$0.0	(\$3,753.8)
Increased Retiree Health Costs	(\$442.5)	(\$442.5)	(\$442.5)	(\$442.5)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	(\$1,770.0)
Years of Service 30yr Cap	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
3% Employee Contribution	\$280.0	\$280.0	\$280.0	\$280.0	\$280.0	\$280.0	\$280.0	\$280.0	\$280.0	\$280.0	\$2,800.0
Eliminate Retiree Dental/Vision	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Hybrid Plan for New Employees	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Replacement Savings at 90%	\$1,066.6	\$853.3	\$640.0	\$426.6	\$213.3	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$3,199.8
GROSS SAVINGS	\$904.1	(\$60.0)	(\$273.3)	(\$486.6)	(\$257.4)	(\$470.8)	\$280.0	\$280.0	\$280.0	\$280.0	\$476.1

**Estimated Fiscal Impact of SB 1227 (H-9)
@ 50% Participation
(in millions)**

	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	Cumulative 10 Year Total
Increase Multiplier to 1.7%	\$0.0	(\$500.5)	(\$500.5)	(\$500.5)	(\$500.5)	(\$500.5)	\$0.0	\$0.0	\$0.0	\$0.0	(\$2,502.5)
Increased Retiree Health Costs	(\$295.0)	(\$295.0)	(\$295.0)	(\$295.0)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	(\$1,180.0)
Years of Service 30yr Cap	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
3% Employee Contribution	\$291.0	\$291.0	\$291.0	\$291.0	\$291.0	\$291.0	\$291.0	\$291.0	\$291.0	\$291.0	\$2,910.0
Eliminate Retiree Dental/Vision	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Hybrid Plan for New Employees	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Replacement Savings at 90%	\$711.1	\$568.9	\$426.6	\$284.4	\$142.2	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$2,133.2
GROSS SAVINGS/(COSTS)	\$707.1	\$64.4	(\$77.9)	(\$220.1)	(\$67.3)	(\$209.5)	\$291.0	\$291.0	\$291.0	\$291.0	\$1,360.7

Notes:

The fiscal information in this summary has been revised based on relevant actuarial data provided by the State Budget Office subsequent to House passage of the bill. Estimates above include assumptions based on 50%, 75% and 100% participation.

- 38,600 employees are currently eligible and 17,200 additional eligibles would be eligible with an 80 and out.
- ORS is currently working on estimating the number of additional employees who are currently eligible for a reduced pension who would be eligible to take the 1.7% percent without reduction under the bill. Increased eligibility could create additional costs/savings.
- Assumes 90% replacement ratios. Replacing fewer employees would create additional savings.
- Tapers replacement savings down over 5 years to assume those retirements would have happened over the next 5 years regardless. Only counts savings directly attributable to the incentives.
- Assumes all participating eligible employees leave prior to July 1 in order to receive a 1.7% multiplier. Costs would decrease to the extent that employees retire between July 1 and October 1 and receive a 1.6% multiplier.
- The bill would create additional savings in reduced unemployment costs if the bill allows employers to avoid layoffs, but the impact is indeterminate.

Fiscal Impact:

While the bill would create savings in the first year, this is because of an actuarial lag such that the added costs of the retirement incentives are not borne by the MPSERS employers until years 2-6. During that period, the incentives create a significant annual net cost, which vary significantly depending on the number of eligible employees that participate. As the participation rate increases, the increased pension and retiree health care costs begin to outweigh the initial replacement savings as well as the long term savings achieved by the 3% employee contribution for retiree health care.