Legislative Analysis

HOUSE FISCAL AGENCY

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MUNICIPAL RETIREMENT REVISIONS

House Bill 5725
Sponsor: Rep. MacGregor

House Bill 5726
Sponsor: Rep. Opsommer

Committee: Appropriations
Complete to 7-16-12

A SUMMARY OF HOUSE BILLS 5725 AND 5726 AS INTRODUCED 6-5-12

House Bill 5725 would amend the Municipal Employees Retirement Act of 1984 to specify that, by a majority vote of its government body, a municipality participating in the Municipal Employees Retirement System (MERS) may (1) revoke its election to have all or some of its employees to be covered by a MERS retirement plan or (2) change the benefit program for all or some of its employees covered by a MERS retirement plan. Changes could include curtailing or eliminating an employee's accrual of future benefits or setting eligibility criteria for an employee to participate in the defined benefit portion of MERS.

The bill would require a municipality revoking its participation in a MERS retirement plan to fund its contribution requirements for accrued financial benefits (i.e., the municipality's portion of the retirement plan's defined benefit unfunded accrued liability), as required by the State Constitution. The amount of those contributions would be determined by an actuarial analysis, to be prepared by an actuary selected by the municipality. The municipality could select the methodology or amortization period to be used to determine annual contributions, but the actuary could not change other actuarial assumptions without the approval of MERS. The retirement system would pay the cost of actuarial analysis from the system's assets.

Under the bill, MERS could not require a participating municipality to participate in another retirement plan administered by the system as a condition of revoking its participation in an existing plan.

House Bill 5726 would amend the Revised Municipal Finance Act to allow a municipality closing a defined benefit (DB) retirement plan and implementing a defined contribution (DC) retirement plan, or a municipality that has already done so, to issue a debt security to pay all or part of the costs of the unfunded accrued liability (UAL) associated with the DB plan. This action could be undertaken by ordinance or resolution of the municipality's governing body, without of a vote of its electors. (With a vote of its electors, the municipality could issue the security pledging its unlimited tax full faith and credit.) The amount of taxes necessary to pay the principal and interest on the security,

together with other taxes levied for the same year, could not exceed the limit authorized by law.

Securities issued under the bill's provisions would be exempted from state and local taxation. A municipality issuing a security would be required to publish a notice of intent, make a comprehensive financial plan containing specified information available to the public, and obtain approval from the state Department of Treasury.

BACKGROUND INFORMATION:

MERS is an independent non-profit public organization that provides retirement plans that Michigan municipalities may adopt for their employees. Prior to the enactment of Public Act 220 of 1996, MERS was operated by the State of Michigan. According to MERS, approximately 750 municipalities—including cities, counties, hospitals, libraries, medical care facilities, road commissions, townships, villages, and other units of local government—participate in MERS, with more than 86,000 individual members and retirees.[1] As of September 30, 2010, net assets for MERS retirement plans totaled $6.6 billion.[2]

FISCAL IMPACT:

The bills would have an indeterminate fiscal impact on local units of government currently participating in MERS or other DB retirement plans.

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Reportedly, municipalities are currently required to hold a local referendum to move employees out of MERS retirement plans under MERS plan documents. To the extent that House Bill 5725 resulted in more municipalities moving employees out of MERS by requiring only a vote of the governing body, financial savings could accrue to those municipalities, depending on the benefit levels and costs of the existing DB plan compared to the costs of the DC or other retirement plan into which employees were moved. (It is possible for a DC plan to have higher employer costs than a DB plan depending on benefit and employee contribution levels.) Moving from a DB plan to a DC plan eliminates risk for future benefits accrued under the DC system, but risk associated with the DB system is not eliminated until a municipality no longer has any employees accruing benefits or retirees receiving benefits remaining in that system.

The bill's provisions regarding required contributions for a municipality's portion of the retirement plan UAL should ensure that MERS assets are sufficient to meet long-term benefit obligations, although the precise methodology or amortization period selected by the municipality could affect the system's financial operations. Generally, government accounting rules provide for accelerated amortization of UAL payments when a DB

[1] http://www.mersofmich.com/index.php?option=com_content&task=view&id=42&Itemid=176
[2] http://mersofmich.com/formfiles/popcafr_2010.pdf

system is closed. There is some risk that a municipality with no employees left in the system would become unable to pay its UAL costs for unforeseen reasons.

Retirement system assets would be reduced by an indeterminate amount in order to pay for individual actuarial analyses for municipalities revoking their participation in MERS retirement plans.

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To the extent municipalities opted to issue securities to pay off the UAL, those municipalities would incur fixed debt obligations, as opposed to retirement system contributions for UAL costs which increase or decrease as investment returns and other factors built into actuarial assumptions fluctuate over time. (New UAL costs could arise over time, beyond those the municipality initially borrows for.) Generally, securities issued for this purpose are not exempt from federal taxation since the purpose of the borrowing is to take advantage of borrowing rates that are lower than assumed rates of returns for DB system investments. The amount of any savings (or costs) to municipalities borrowing under the bill's provisions would depend on the interest rate at which they could borrow funds relative to future retirement system investment returns.

The bill may create some administrative costs for the Department of Treasury to review and approve the issuance of securities allowed under its provisions.

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■ 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.