Legislative Analysis

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PUBLIC SCHOOL RETIREMENT REVISIONS

Senate Bill 1227 (CR-1)
Sponsor: Sen. Jud Gilbert
House Committee: Oversight and Investigations
Senate Committee: Appropriations

Complete to 5-13-10

A SUMMARY OF SENATE BILL 1227 (CR-1)

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 before September 1, 2010. Retirees would have to apply before June 11, 2010 and would have until June 11, 2010 to withdraw their application.

In addition, for members who retire by September 1, 2010 the bill would provide a 1.6% multiplier in the pension formula for an employee who is eligible to retire under current eligibility and a 1.55% multiplier for members who qualify under the 80 and out. Currently a member's pension calculation equals their final average compensation (FAC) multiplied by their years of service multiplied by 1.5%. The bill would cap the final average compensation to which the additional multiplier was applied at $90,000.

The bill would allow for a superintendent or chief administrator to provide an extension to allow an employee to remain until September 1, 2011. Each reporting unit would be allowed to grant 1 extension. Another 2,500 extensions would be available statewide to be distributed on a prorata basis by the Office of Retirement Services.

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 July 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 would have to contribute 1.5% for FY 2010-11 but would contribute 3.0% in subsequent years.

Funds deposited in the irrevocable trust would be used to pay for retirement health care benefits for retirees and their eligible dependents.

Hybrid Plan for New Employees

The bill would move all newly hired school employees after July 1, 2010 into a hybrid pension and defined contribution system. The pension would be similar to the existing MIP plan with the following changes:

- Increase final average compensation period from 3 years to 5 years, which will decrease the final average compensation for most employees.
- Increase the minimum retirement age to 60 with 10 years of service (currently minimum age for Basic plan is 55 and the MIP plan has no minimum age with 30 years of service).
- Prohibit the purchase of service credit to meet service requirements.
- Eliminate cost of living adjustments to pension allowances.
- Provide a defined contribution benefit (Tier 2) with a 50% employer match on a maximum employee contribution of 2% of salary, for a maximum employer contribution of 1%. An employee would automatically be enrolled with the maximum contribution of 2% unless they affirmatively elect not to contribute or contribute a lesser amount. An employee would also be allowed to contribute additional funds without the match and subject to Department of Technology, Management, and Budget and the Internal Revenue Code. The employee would vest in the employer match as follows: 50% after 2 years of service, 75% after 3 years of service, and 100% after 4 years of service.

  In addition, individual employers could negotiate higher contributions up to a maximum of a 50% employer match on an additional employee contribution of 4% of salary, for a total maximum employer contribution of 3%. Additional employer contributions and matches would be subject to negotiations for both employees in the new hybrid plan as well as those in the Basic Plan and the current Member Investment Plan.

- Provides for a regular interest rate for the Hybrid of between 0% and 7%, and assumes a rate of return of 7%.
- Would allow other entities that receive direct or indirect funding from the School Aid Fund to opt into the new hybrid system.

Rehired Retirees

For retirees who retire after July 1, 2010 and work directly for a MPSERS reporting unit, the bill would allow them to maintain pension and health benefits if they earn less than 1/3 of their final average compensation. If they earn more than 1/3 of their final average compensation, their pension and health care benefits would be suspended until the employment ends.

For those retirees who retire after July 1, 2010 and afterward perform core services for a MPSERS reporting unit but who are employed independently or by a third party, the bill would suspend their pension and health care benefits.

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:

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 and allowing for an 80 and out could cost $2.2 billion at a 50% participation rate. The costs would be distributed over the next 6 years, but would potentially be partially offset by an estimated $1.7 billion in savings from replacing fewer employees and due to the salary differential for new employees.

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.

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 $300 and $409 million depending on the year and could total between $3.5 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.

Rehired Retirees

Suspending pension and retiree health benefits for retirees who return to work for a reporting unit (who earn more than 1/3 of their final average compensation if now employed directly for a reporting unit or who make any portion of their previous salary if employed by a third party or independently employed) would create a savings to the pension system. However, there are no data available to determine the fiscal impact of these provisions.

Ten-Year Net Savings/Costs

See the attached table for a ten-year analysis of projected net savings/costs of the bill with participation assumptions of 50%. The estimated net savings/costs would range from a savings of $104 million to $680 million depending on the year as the added pension and retiree health care costs are paid off and the long term savings from the 3% contribution remains. Estimated savings over ten years would be $3.15 billion.

ORS Appropriation

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

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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.

School Employee Pension Reforms: 10-Year Estimated Savings Analysis of S.B. 1227 (CR-1)
(in millions)

	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16	FY 17	FY 18	FY 19	FY 20	Cumulative Savings TOTAL
Increase employee contribution rate savings	$300.0	$310.6	$321.4	$332.6	$344.2	$356.4	$368.7	$381.6	$395.1	$409.1	$3,519.7
Revised hybrid plan for new employees savings	1.2	4.0	6.5	8.9	11.3	13.8	16.5	19.4	22.4	25.4	129.4
Retirement incentive – pension cost	0.0	(251.5)	(251.5)	(251.5)	(251.5)	(251.5)	0.0	0.0	0.0	0.0	(1,257.5)
Increased health care costs on pension system	(295.0)	(295.0)	(295.0)	(100.0)	0.0	0.0	0.0	0.0	0.0	0.0	(985.0)
Wage savings	673.4	530.6	375.8	163.6	0.0	0.0	0.0	0.0	0.0	0.0	1,743.4
Estimated Gross Savings	**$679.6**	**$298.7**	**$157.2**	**$153.6**	**$104.0**	**$118.7**	**$385.2**	**$401.0**	**$417.5**	**$434.5**	**$3,150.0**

Source: House and Senate Fiscal Agencies

Assumptions:
--50% participation rate
--90% replacement rate
--Wage savings accrue only during years retirees otherwise would have remained working