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EARLY RETIREMENT INCENTIVES

House Bill 5353 as passed by the House
Second Analysis (3-13-92)

Sponsor: Rep. Justine Barns
Committee: Senior Citizens and Retirement

THE APPARENT PROBLEM:

The reduction in revenues resulting from the continuing recession could make fiscal year 1992-93 a very difficult one for the state. New ways to reduce state spending must be sought. One method that has been widely and successfully employed in the private sector is a reduction in payroll expenses through a program of early retirement. An early retirement program induces senior, relatively well-paid employees, who are either eligible for retirement, but do not choose to retire, or who are just short of retirement eligibility, to retire during a designated "window period." The inducement is accomplished through financial incentives. While this makes their retirement comparatively expensive for the employer, it produces overall savings because, in a well-managed program, the retiring employees are not replaced or are replaced to a limited extent with younger, less well-paid employees. Such a program can avoid the necessity of layoffs and positively affect morale by permitting the advancement of younger employees and enhancing the success of affirmative act programs. Public Act 62 of 1990 amended the State Employees Retirement System to establish such a window period, by providing a "70 and Out" retirement option, between October 1, 1991, and April 1, 1992, for employees who were at least 50 years old, and whose combined age and years of credited service equalled 70 years. However, although it is estimated that some 1,400 employees retired (or will retire) under this option, it is claimed that many more employees fell just short of either the age or length of service eligibility requirements. It is argued that, if the age 50 requirement were eliminated, and if a grant of 5 years of service were credited to a member who retired during the window period, some 1,800 additional employees would then be eligible to take advantage of this early retirement opportunity.

THE CONTENT OF THE BILL:

Under ordinary circumstances, a member of the State Employees Retirement System (SERS) is eligible to retire with a regular (unreduced) retirement allowance at age 60 with 10 years of service credit, or at age 55 with 30 years of service credit. In addition, Public Act 62 of 1991 established a "window" period, beginning October 1, 1991, and ending April 1, 1992, during which a state employee, whose age and years of credited service total at least 70, may retire with full benefits at age 50. House Bill 5353 would amend the State Employees' Retirement Act to extend the "window" period to May 1, 1992. Under the act, members are required to file an application stating a retirement date, which must be 30 to 90 days after the application's filing, but not later than March 1, 1992; under the bill, this date would be extended to April 1, 1992.

70 and Out Plan. House Bill 5353 would amend the act to delete the requirement that a member must be 50 years of age to be eligible for retirement during this "window" period. The bill would also provide for a grant of 5 years of service credit to a member who retired during this window period. The member's retirement allowance would be recalculated to include the additional years of service credit, and the recalculated allowance would be payable effective the first day of the month following the recalculation.

Supplemental Members. The bill would also delete the age 50 requirement and grant 5 years of service credit to supplemental members -- those employed in "covered positions" in state correctional facilities and in psychiatric forensic centers -- who chose to retire during this "window" period, provided that the member's last 3 years of credited service, not including the 5 years of service granted under the bill, were "covered" service. Under the bill, a supplemental member's retirement allowance would be computed in the same manner as a temporary straight life supplemental early retirement allowance is computed at present. The allowance would be in an amount equal to the difference between: i) 2 percent of the member's supplemental final average compensation (FAC) multiplied by years of "covered" service, plus 1.5 percent of the member's FAC multiplied by the excess, if any, of the member's credited service over covered service; and ii) a regular retirement allowance. (The 5 years of service granted under the bill would be considered "covered" service for the purpose of computing the member's retirement benefit).

Conservation Officers. Public Act 110 of 1990 established an early retirement period, beginning May 1, 1991, and ending July 1, 1992, which permits a member to retire at age 50, provided that the member has at least 10 years of credited service as a conservation officer, including the last 2 years before retirement. House Bill 5353 would delete the age 50 requirement and grant 5 years of service credit to conservation officers who chose to retire during the October 1, 1991 to May 1, 1992 "window" period, provided that the member's last 2 years of credited service, not including the 5 years of service granted under the bill, were as a conservation officer. A conservation officer who retired under the provisions of the bill would be eligible to retire with a regular retirement allowance, which, for conservation officers, is equal to 2 percent of the member's annual compensation for the most highly compensated 24 consecutive months of service as a conservation officer, times the number of years of credited service.

Legislative Employees. Public Act 62 also established two additional early retirement periods following the 1992 and 1994 elections for legislative employees. House Bill 5353 would also delete the age 50 requirement and grant 5 years of service credit to legislative employees who chose to retire during these "window" periods, and would amend the language of the act to clarify that these provisions apply only to employees of the legislative branch who are constitutionally excepted or exempt from the classified state civil service.

Universal Service Credit Buy-In. The act allows members, under certain circumstances, to purchase service credit for various types of public employment or for periods of time that cause interruptions or delays in employment. Beginning on the effective date of the bill, a member could elect to purchase up to 5 years of nonspecific service credit at actuarial cost, as defined under the bill, minus the years of service credit purchased under certain other provisions of the act. Service credit purchased under this provision could not be used to satisfy the minimum number of years of service credit needed to be vested in the retirement system. Under the bill, should a member who had paid for this purchase die, or leave state employment before receiving a retirement allowance, then the payment would be refunded to the member or to the beneficiary, legal representative, or estate. (Note: Under the bill, a member would have until January 1, 1993, to purchase service credit for all other buy-ins, with the exception of maternity-paternity, military service, and the above universal buy-in.)

The bill would amend the definition of "actuarial cost" under the act to mean an amount that a member would have to pay to purchase additional service credit. Under the bill, "actuarial cost" would equal the product of: a) a percentage, equal to the average actuarial present value of additional benefits that the credit of one additional year of service would produce; b) a member's compensation; and c) the number of years of credited service purchased.

Amortization. The bill would amend the act's amortization schedule to provide that the cost of the early retirement provisions would be amortized (paid for) over a 30-year period, rather than over 10 years.

MCL 38.1 et al.

FISCAL IMPLICATIONS:

Estimates of the savings that would result from the additional retirements induced by House Bill 5353, as it was reported from the House Senior Citizens and Retirement Committee, varied. The House Fiscal Agency estimated that 2,098 additional members would retire, resulting in a savings of $3.9 million for 1992, and $20.8 million for 1993, if a 30-year amortization schedule were used. The Retirement Bureau used a 10-year amortization schedule, and estimated that 1,520 additional members would retire, resulting in a savings of $5.9 million for the first year. No estimates are available for the savings that would be produced by House Bill 5353 as passed by the House. (2-13-92)

ARGUMENTS:

For:

Employees who have given years of service to the state deserve to be given the choice of leaving with dignity, rather than being laid off. The bill would accomplish this by producing a reduction in force for state employees by voluntary retirement, rather than forced layoffs. The bill would also produce savings for the state in a time of special need. Senior, relatively well-paid employees -- who are either eligible for retirement, but do not choose to retire, or who are just short of retirement eligibility -- would retire under the "70 and Out" program, and either would not be replaced, or would be replaced with younger, lower-paid employees. In addition, the programs would positively affect morale by permitting the advancement of younger employees.

For:

The bill would alter the method by which actuarial costs are currently calculated in figuring out the employee cost of purchasing service credits. Rather than base calculations solely on the salary of the employee in question, future calculations would be based on salary <u>and</u> age, resulting in a more accurate prediction of actual costs. This would produce a higher cost to the employee, but no cost to the retirement system. Other savings to the state would be gained from the bill's provision to permit a member to purchase up to 5 years of nonspecific service credit at actuarial cost, while at the same time phasing out the myriad of other buy-ins (with the exception of those for maternity-paternity leave, and for military leave) that are currently available. This provision would reduce the administrative costs involved in handling these options.

For:

For the past year, many state employees have lived with the uncertainty of not knowing if, or when, they would be laid off. At the same time, rumors have circulated that early retirement programs would be introduced that would induce into retirement those who are old enough to retire from state employment, and who are young enough to enter a second career. If more employees were allowed to retire, the state's ability to avoid the disruption and economic hardship generated by layoffs would be enhanced, and employees would have an opportunity to make plans for the future.

Against:

House Bill 5353 would change in mid-course the existing early retirement program initiated under Public Act 62 of 1991. In view of the current recession, the object of the present administration is to downsize state government. One element of this policy included the early retirement provisions of Public Act 62, which provided for an early retirement "window" period ending April 1, 1992 for employees who had reached 50 years of age, and whose combined age and amount of credited service equalled 70 years. It was estimated by the Retirement Bureau that 1,500 employees would apply for early retirement under this program, and, as of January 12, 1992, 1,256 persons had applied. It is obvious, therefore, that the program is working. To change this program in mid-course would send a signal to employees that, if they wait long enough, more incentives will be added to make early retirement even more palatable. In addition, under federal law, early retirement programs must treat those similarly situated in a similar fashion. Therefore, the provisions of House Bill 5353 would have to be offered to all who are eligible for early retirement (including those who have already applied, under the provisions of Public Act 62) retroactively.

Against:

The benefits offered in House Bill 5353 are needlessly generous. A person retiring before age 60 with less than 30 years of service ordinarily suffers a reduction in allowance of one-half of one percent for each month he or she is less than 60. To remove this penalty is a significant incentive in itself. A satisfactory reduction in force could be obtained without offering the five-year service grant as an incentive. In addition, the majority of those state employees who would be eligible to retire under the bill are not in danger of losing their jobs, since, by the time an employee approaches 50 years of age or acquires 20 or more years of employment, he or she has usually acquired "bumping" rights.

POSITIONS:

The Retirement Coordinating Council supports the bill. (3-12-92)

The Michigan Association of Governmental Employees (MAGE) supports the bill. (3-12-92)

The United Auto Workers, Local 6000, supports the bill. (3-13-92)

The Michigan Corrections Organization/SEIU Local 526M supports the bill. (3-12-92)

The Office of the State Employer opposes the bill. (3-12-92)

The Retirement Bureau in the Department of Management and Budget opposes the bill. (3-13-92)