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UNIV. EMPLOYEES' RETIREMENT

House Bill 4047 as enrolled
Public Act 272 of 1995
Second Analysis (1-4-96)

Sponsor: Rep. Kim Rhead
House Committee: Appropriations
Senate Committee: Appropriations

THE APPARENT PROBLEM:

Michigan's Public School Employees Retirement System (PSERS) Act currently includes under its provisions seven of the state's public universities (Eastern, Western, Northern, Central, Michigan Technical, Lake Superior State, and Ferris State); thus, employees of these institutions who qualify are members of PSERS. However, under the Optional Retirement Act of 1967, certain full-time employees of these institutions may opt out of PSERS into a different retirement system. (Employees of the state's eight other universities--Michigan, UM-Dearborn, UM-Flint, Michigan State, Wayne State, Grand Valley State, Oakland, and Saginaw Valley--are exempt from the PSERS Act and are covered under the individual retirement systems of their respective employers.) In recent years, the cost to these seven universities for mandated participation in MPSERS on behalf of participating employees has generally been higher than that paid by the state's eight other public universities. For example, the coverage required under MPSERS resulted in the seven member schools paying, for fiscal year 1993-94, 14.41 percent of their entire payroll for employee retirement costs; for the same year, the other eight schools' retirement contribution was only ten percent. Officials of these schools note that, though employee retirement costs for fiscal year 1994-95 fell to just over 11 percent of payroll due to a one-time credit from MPSERS, costs have been steadily rising, and--for at least one of the schools--may surpass 18 percent of payroll by 1997. This disparity in what the seven schools required to participate in MPSERS pay for retirement, compared to that paid by the other eight, leaves them at a competitive disadvantage in attracting students since the higher retirement costs generally must be offset either by proportional increases in state funding (via the appropriations process) or with higher tuition fees. As the state generally has held increases in amounts allocated for higher education to under the rate of inflation, these universities have requested legislation that would exclude from membership in MPSERS any employees hired by them after January 1, 1996.

THE CONTENT OF THE BILL:

The bill would amend the Public School Employees Retirement Act to exempt the seven universities currently covered by the act and their future employees from participation in the act. The bill specifies that, beginning January 1, 1996, "out of system public education service" would mean, among other things, service performed at any of the state's public institutions of higher education. New employees of the seven universities hired after January 1, 1996 would not be members of the retirement system, and after this date the term "reporting unit" would not include a university unless it had employees on its payroll who were members of MPSERS.

For fiscal years that began on or after the bill's effective date, the retirement system would have to determine a separate contribution rate for the universities affected by the bill, as prescribed by current law, except that the unfunded actuarial accrued liability would be amortized as a level dollar amount in 40 annual payments. The amount of the unfunded accrued liability on which the separate contribution rate was determined would be that amount which a university was legally responsible for and would be calculated by actuarial analysis. Any reduction in the unfunded liability of the system pursuant to governmental action that affected the entire system would be allocated to all reporting units including universities as determined by the system's actuary.

MCL 38.1305, 38.1306, and 38.1307

FISCAL IMPLICATIONS:

The House Fiscal Agency says that, under the bill, the seven universities currently required to participate in MPSERS would realize cost savings which would depend on the rate of employee turnover after the bill became law, the type of retirement program, if any, that was selected for new employees, and the outcome of the Musselman case, currently pending before the state supreme court, involving funding of health benefits for school employees. Assuming these universities had employee turnover of five percent, which is the rate for filling vacant positions, that another retirement system was adopted, and that the supreme court allowed cash funding of health benefits (rather than prefunding, which is the issue in the case), the seven schools could realize a combined annual savings of between $685,000, an amount that would accumulate until all university employees no longer were members of MPSERS. They could realize savings of up to $1.486 million in the bill's first year of implementation if the court decision required prefunding of health benefits. And additional savings could be realized to the extent the universities did not provide any retirement plan for certain employees. These savings would be offset or reduced by the amount that MPSERS determined each university would have to pay to retire its portion of the MPSERS unfunded accrued liability. (1-3-96)

ARGUMENTS:

For:

Seven state public universities--that is, Central Michigan, Eastern Michigan, Ferris State, Lake Superior State, Michigan Technical, Northern Michigan, and Western Michigan--are all currently required to enroll some of their full-time employees and all part-time and temporary employees in the Public School Employees Retirement System, known as MPSERS. Full-time employees at these schools may choose to participate in another retirement system, as allowed under the Optional Retirement Act, and most (nearly 86 percent), in fact, have opted into the Teachers' Insurance and Annuities Association-College Retirement Equities Fund (TIAA-CREF) over the last five years. This alternative system is a defined contribution plan, where both employees and employers contribute a portion to retirement. However, universities whose employees are enrolled in TIAA-CREF generally have lower pension costs than those whose employees must be enrolled in MPSERS, which--assuming all receive the same funding from the state--enables them to keep tuition costs lower. This disparity would be resolved by the bill, which provides that employees hired by these seven schools after January 1, 1996, would not have to be enrolled in MPSERS; instead, the boards at these universities could choose to enroll these employees in any retirement system, or perhaps none, just as other university boards currently decide this matter for their respective schools. (Those employees who were members of MPSERS prior to this date would continue as enrollees in this system.) Most of the eight other schools currently enroll their employees under TIAA-CREF, and it is expected that the seven universities affected by the bill would do the same. Based on estimates provided by the House Fiscal Agency, the seven universities could realize combined savings of close to $1 million in the first year the bill took effect, and somewhere between $250,000 and $500,000 annually in subsequent years depending on the rate of employee turnover. Without the bill, retirement costs for these schools could, in only a few short years, increase to a level nearly double what other schools currently pay under the TIAA-CREF program.

For:

The bill would require MPSERS to calculate the unfunded liability in the retirement system that was attributable to each university, and each would be required to retire their respective amount in level payments over 40 years. This would both protect the system's ability to support future retirees and ensure that each school would pay only its fair share of the total unfunded liability.

Against:

The bill provides no guarantees that employees currently enrolled in MPSERS would be enrolled in a comparable retirement program, or even any at all. Even if they were, the new program probably would not provide the same level of benefits currently offered by MPSERS. Because it is a defined benefit plan, MPSERS generally provides a more secure retirement option than defined contribution plans. Under defined contribution plans, employees usually decide how to invest their own retirement funds, whereas an investment professional performs this job in a defined benefit plan. Also, removing these university employees from MPSERS could harm its financial integrity by reducing the number of people paying into the system, and by encouraging other plan participants to opt out, too. At the very least, the bill should be amended to give all universities--including, possibly, those whose employees are not currently enrolled in MPSERS--the option of participating in MPSERS.

Response:

All other universities provide some form of retirement plan to their employees, some with contributions rates similar to that required under MPSERS, and the seven affected by the bill would have an incentive to provide something similar if they wanted to attract the best employees. Defined contribution plans are not necessarily riskier than defined benefit plans, as they could provide a comparable retirement package at a lower cost (because an investment manager is not used) as long as an employee used common sense by investing in a diverse number of financial instruments. Also, an employee in a defined contribution plan becomes vested immediately, and such plans are easily portable if an employee leaves to work elsewhere. Meanwhile, arguing that the seven universities, or any of them, ought to have the choice of enrolling their employees in MPSERS seems nonsensical since they, in fact, are the ones who requested the legislation.