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SFA BILL ANALYSIS

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House Bill 5732 (as enrolled)
Sponsor: Representative Paul DeWeese
House Committee: Senior Health, Security and Retirement
Senate Committee: Appropriations

Date Completed: 3-28-02

CONTENT

The bill would amend the State Employees' Retirement Act to provide an early-out retirement plan for State employees who met certain qualifications. The bill also would create the Health Advance Funding Subaccount, which would provide for the prefunding of health benefits when that account reached fully-funded status. In addition, the bill would revise duty and non-duty disability provisions, make changes to ensure that the retirement system remained in a tax-exempt status, and change the compensation rate of retirement board members.

Current Law Provisions

Members of the State Employees Retirement System's (SERS's) defined benefit plan are entitled to retire with full retirement benefits upon meeting the age and service requirements. Currently, those requirement are:

- Age 60 with 10 or more years of credited service (or five years in certain circumstances); or,
- Age 55 with at least 30 years of credited service; or
- Age 55 with at least 15 but less than 30 years of credited service. (The pensions for these early retirees, however, are permanently reduced by .5% for each month a member is less than age 60.)

A pension under current law is calculated by multiplying 1.5% by the final average compensation (FAC), times the years of credited service. The FAC is determined by the three consecutive years of service that return the highest average.

Proposed Early-Out Provisions

The bill proposes an early-out provision for most members of SERS. To be eligible, a member would have to have been employed by the State (or be on layoff status) for the preceding six-month period ending on the effective date of his or her retirement. Members who would be eligible for this early-out retirement plan are classified Civil Service employees, unclassified Civil Service employees, employees of the judicial and legislative branches who are not judges or legislators, employees of the Governor's office, employees working in covered positions who are otherwise not eligible after July 1, 2002, for a supplemental early retirement for covered employees under current law, and employees employed by the former Department of Mental Health who went on layoff status before January 1, 1997. Members who would be exempt from taking an early-out retirement under this proposal are those working as conservation officers and those working in covered positions who do qualify for a supplemental early retirement for covered employees as specified. (Covered employees are generally those working within the confines of a secure correctional facility.)

To qualify for an early-out retirement under the bill, a member would have to have a combined age and length of credited service that equaled at least 80 ("80 and out") as of November 1, 2002, or on the effective date of retirement, whichever would be earlier. There would be no minimum age requirement so long as the member met the 80 points. Members meeting these requirements would receive full retirement benefits the same as traditional retirees under current law, with one exception.

Members choosing to retire early under this proposal would receive an enhanced multiplier of 1.75%, rather than the 1.5% under current law as mentioned above. Thus, the retirement calculation for an employee taking an early retirement under this proposal would be:

1.75% times FAC times
years of credited service

To file for an early-out retirement, members would have to submit an application to the Office of Retirement Services between April 1 and April 30, 2002, and state a retirement date between July 1, 2002, and November 1, 2002. Members filing an application also would be able to withdraw that application for any reason until May 15, 2002; after that date, the application would be irrevocable.

Finally, members of SERS who transferred from the defined benefit plan to the defined contribution plan and met the "80 and out" requirements also would be eligible for this early-out retirement plan. However, these members would receive a benefit based only on 0.25% of FAC times years of credited service.

<u>Extension of Retirement Date and Lump Sum Payments</u>

Individuals eligible for the early-out retirement plan would be able to extend their retirement date up to 15 months (no later than February 1, 2004) from the original dates set forth in the proposed legislation. Members could extend their retirement dates provided that an extension was requested by their department director or designated by the Legislature or the judiciary. Requests for extensions for executive branch employees would have to be submitted to, and approved by, the Office of the State Employer and the State Budget Office by May 31, 2002. Legislative and judicial employees would have to submit their requests to the Office of Retirement Services by May 31, 2002; however; approval would be granted by legislative leaders or the chief justice, as applicable, or the director or chair of the Legislative Retirement System (LRS) for an employee of the LRS. In addition, members who requested an extension that was ultimately rejected would be allowed up to seven days after that rejection to withdraw their application for retirement.

The bill also would provide for the payment of both accrued sick leave and accrued annual leave. Accumulated sick leave would be paid in monthly installments over a period of five years, while accrued annual leave would be paid in a lump sum on or after October 1, 2002. The bill specifies that sick leave payments received under this provision could not be used for the purchase of service credit. In addition, the bill specifies that payments for sick leave and annual leave would not be considered pensions and would be taxable and subject to execution, garnishment, and attachment, and would be assignable as provided in the Act.

<u>Provisions Not Related to the Early-Out Retirement Plan</u>

In addition to the early-out retirement plan provisions, the bill contains provisions not related to the early-out retirement plan. These changes are as follows:

- <u>Health Advance Funding Subaccount</u> - The bill would create the Health Advance Funding Subaccount for the purpose of receiving deposits in years when the assets for normal retirement benefits are funded at 100% or more. In years when normal costs are fully funded, employer contributions could be deposited into the new subaccount. Funds from the subaccount could not be spent until the actuarial liability for health benefits was fully funded. Also, the Department of Management and Budget, with the approval of the Senate and House Appropriations Committees, would be permitted to transfer amounts from the Health Advance Funding Subaccount to the employer's accumulation fund (the fund set aside for the pensions of future retirees) to cover any underfunding that might arise for normal retirement costs.

- <u>Duty and Non-Duty Disability Pensions</u> - The bill would establish a deadline for application for disability pensions of 12 months after the employee had separated from State service. A member could file an appeal to the retirement board to allow up to 24 months for application if "good cause" were determined. Current practice has been to allow up to 24 months from the date of separation from State service; however, there is no statutory provision for doing so.

- Medical Examinations - Currently, disability retirees under age 60 are required to undergo a medical examination to determine disability once per year for the first five years of retirement, and at least once every three years thereafter. The bill would eliminate this requirement and specify instead that the retirement board could require a person to be examined at any time, but not more than once per year.

- Survivor Benefits for Minors - The bill would allow the pension benefits of deceased members to be paid to minor children until age 18 if there were no surviving spouse.

- Arrangement and Fund - The bill would allow the retirement system to create an Arrangement and Fund pursuant to the provisions in House Bill 5108 that would allow benefits that exceed the IRS limits to be paid to retirees. The Internal Revenue Code limits the amount of pension that may be paid to a retiree from pension assets; thus, in order to pay a retiree the amount of pension (that he or she is entitled to receive) that exceeds the IRS limits, the retirement system would have to establish an Arrangement and Fund consisting of nonpension assets.

- Additional Changes - The bill would make several other changes, including: the deletion of references requiring the specification of a retirement date that is at least 30 days but not more than 90 days after the filing of an application; changes to ensure that the retirement system remains in a tax-exempt status; a provision that would allow former employees of the City of Detroit to purchase service credit for that service; and a change to the amount of per diem reimbursement for board members from $35 to an amount established annually by the Legislature.

- Tie-Bar - This bill is tie-barred to House Bill 5109, which would amend the State Employees' Retirement Act to specify that benefits under the Act would be subject to the Public Employee Retirement Benefit Protection Act (proposed by House Bill 5108), as well as provide the appropriation necessary to pay for the administrative costs associated with this bill.

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FISCAL IMPACT

Current Department of Management and Budget estimates indicate that approximately 8,800 State employees would be eligible to retire under this early-out plan, with an average annual salary of $68,600. Of those eligible, it is estimated that 5,300 would take advantage of this option and retire early. The Governor's plan calls for a replacement ratio of one to four, meaning that for every four employees who retired, only one eventually would be replaced, on average. Thus, all cost estimates take these factors into account.

Based on the salaries and the number of employees anticipated to retire early under this proposal, the State would realize an annual saving in salaries of $364 million. After the subtraction of all costs, such as health insurance, accumulated sick leave, and accumulated annual leave, the replacement of one in four employees, and the increase in pension liabilities for these new retirees, the State would realize a net GF/GP saving of $58 million annually.

Following is a table indicating the number of employees in each State department and the number of employees in each department eligible for this early-out retirement plan.

Fiscal Analyst: Joe Carrasco, Jr.

ELIGIBILITY FOR EARLY-OUT RETIREMENT PLAN BY DEPARTMENT OCTOBER 31, 2002

Department/ Agency	Number of Un/Classified Employees	Number of Eligible Employees	Percent of Eligible Employees
Executive Office	70	2	2.9%
Auditor General	175	24	13.7
Management & Budget	1,519	273	18.0
MI Strategic Fund	268	51	19.0
Attorney General	556	122	21.9
Civil Rights	168	53	31.5
Civil Service	197	44	22.3
State	2,025	322	15.9
History, Arts & Libraries	215	30	14.0
Gaming Commission	87	0	0.0
Lottery	186	37	19.9
Treasury	1,485	312	21.0
Education	385	85	22.1
Community Health	4,808	1,036	21.5
Family Independence	13,041	3,045	23.3
Corrections	7,691	422	5.5
Military and Veteran's Affairs	996	127	12.8
State Police	1,090	171	15.7
Transportation	3,105	662	21.3
Consumer & Industry Affairs	2,659	626	23.5
Unemployment Agency	1,129	405	35.9
Natural Resources	1,535	306	19.9
Environment Quality	1,563	223	14.3
Agriculture	632	109	17.2
Career Development	797	193	24.2
Employment Services	297	82	27.6
Legislative	1,219	13	1.1
Judiciary	1,385	109	7.9
TOTAL	**49,283**	**8,884**	**18.0%**

Source: Department of Management and Budget

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.