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BILL ANALYSIS

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Senate Bill 524 (as introduced 5-23-07)  
Sponsor: Senator Bruce Patterson  
Committee: Judiciary

Date Completed: 12-4-07

### **CONTENT**

**The bill would amend the Judges Retirement Act to do all of the following:**

- Require the Judges Retirement System annually to increase a retirement allowance by up to \$900, if the actuarial value of the assets in Tier 1 exceeded the present value of expected future benefit payments for Tier 1 beneficiaries.**
- Provide for an annual 67% supplement for a retirant or beneficiary of a deceased retirant under Tier 1 if the retirant could not purchase service credit for military service because he or she had been prevented from accumulating 12 years of credited service due to the mandatory retirement age for judges.**
- Provide that the recalculated retirement allowance would be the basis for the calculation of future adjustments; the Act's final compensation limits would not apply to the bill's retirement allowance supplements; and, for a retirant or beneficiary receiving more than one retirement allowance, the supplements could be received only on the largest allowance.**
- Specify that, if a retirant died before the end of 2007, and benefits did not otherwise become payable to a beneficiary, his or her retirement allowance could not be supplemented under the bill.**

("Tier 1" is the Judges Retirement System's defined benefit program. The system's defined contribution system is known as "Tier 2".)

#### **\$900 Maximum Annual Supplement**

Under the bill, effective July 1, 2007, the retirement allowance payable to a retirant or beneficiary of a deceased retirant under Tier 1 annually would be supplemented by the amount determined below.

By April 1 of each State fiscal year, the retirement system would have to determine the amount by which the actuarial value of the assets in Tier 1 exceeded the present value of expected future benefit payments for Tier 1 beneficiaries. If the excess amount would allow retirants and retirement allowance beneficiaries to receive individual increases of \$900 per year, the retirement system would have to grant an annual increase of that amount to each retirant and retirement allowance beneficiary receiving retirement payments under the Act. In any year in which the actuarial value of assets exceeded the present value of expected future benefit payments by less than \$900 per retirant, the increase would have to be reduced on a pro rata basis to reflect an amount less than \$900 per retirant. If the actuarial value of assets did not exceed the present value of expected future benefits, no increase could be given for that year.

## Military Service Credit Annual Supplement

Under the bill, effective July 1, 2007, the retirement allowance payable to a retirant or beneficiary of a deceased retirant under Tier 1 annually would be supplemented by 67% if all of the following applied to that retirant:

- He or she potentially was eligible to purchase two years' service credit under the Act, the former Judges Retirement System, or the former Probate Judges Retirement System, because he or she served honorably on active duty as a member of the U.S. Armed Forces.
- He or she was unable to purchase the military service credit while a member because he or she had not accumulated 12 years of credited service.
- He or she was older than 60 years of age when entering the system and was prevented from accumulating 12 years of credited service by the mandatory retirement age for judges specified in the State Constitution.

(Article VI, Section 19(3) of the State Constitution provides: "No person shall be elected or appointed to a judicial office after reaching the age of 70 years.")

## Application of the Supplements

The recalculated retirement allowance under the bill would be the basis on which future adjustments to the retirement allowance were calculated. The percentage of final compensation limits of Section 503 of the Act would not apply to the increases authorized by the bill. (Section 503 establishes the formulas for determining a retirant's retirement allowance, and includes maximum limits on that allowance expressed as a percentage of the retirant's final compensation.)

For a retirant or beneficiary of a deceased retirant who was eligible to receive either supplement, who was receiving a retirement allowance pursuant to service credited under the former Judges Retirement System, and who was receiving a retirement allowance pursuant to service credited under the former Probate Judges Retirement System, the retirement system could supplement only the largest retirement allowance.

If a retirant died before December 31, 2007, and no benefits became payable under Section 506 or 508 of the Act, the retirant's retirement allowance could not be supplemented under the bill. (Sections 506 and 508 allow a member or vested former member to elect to receive a retirement allowance for life or receive for life a smaller allowance that is continued to a beneficiary upon the retirant's death.)

Proposed MCL 38.2513 & 38.2514

Legislative Analyst: Patrick Affholter

## **FISCAL IMPACT**

The bill has two distinct purposes: 1) to provide an annual supplement to all retirants' pensions if the value of the Judges Retirement System's (JRS's) assets exceeded the amount necessary to pay all anticipated future benefits, and 2) to increase by 67% the pension of a retirant who served on active duty in the Armed Forces, was unable to purchase allowable service credit because 12 years of service in the judicial branch had not been completed, and was not able to complete those 12 years of service because the person entered the system after age 60 and was mandated to retire at age 70 pursuant to the State Constitution.

Addressing the first purpose of the bill (found in proposed Section 513), it is anticipated that the State would experience a fiscal impact when the actuarial value of the assets in the pension system exceeded the present value of expected future benefit payments (i.e., when

the system was considered "overfunded" by this actuarial measure, which differs from measuring the funded percentage via the ratio of actuarial assets to accrued liability). In those years, retirants and their beneficiaries would receive individual increases of up to \$900 per year. If the actuarial value of assets did not exceed the present value of expected future benefits, no increase would be given for that year.

It appears as though the legislation would build the up-to-\$900 annual increases into the base pensions (under subsection (4) of Section 513). Thus, there would be an adverse fiscal impact on the State if the value of the assets in the system fell below the amount necessary to pay its obligations (which would grow if \$900 increases were provided to pensions) and any "cushion" that would have existed in the system from overfunding had already been used up to provide the \$900 annual increases.

In recent years, employee (judges') contributions have covered most of the JRS's obligations. The State contributed nothing between FY 1997-98 and FY 2004-05, a little over \$600,000 in FY 2005-06, and just under \$200,000 in FY 2006-07. State contribution, when needed, is statutorily designated to come from 24% of the Civil Filing Fee Fund. This portion of the Civil Filing Fee Fund otherwise goes to the Court Equity Fund and the Court Fee Fund. The first \$2.2 million goes to the Court Equity Fund, which makes payments to local trial courts for operational expenses. The remaining amount, which has been approximately \$7.1 million in recent years, is used to pay judicial salaries. If additional Court Fee Fund dollars went into the JRS to pay for these \$900 adjustments, then additional GF/GP support would be required to fund the judicial salaries. Also, funds would not necessarily be available for transfer to the Court Equity Fund.

According to the 2006 Comprehensive Annual Financial Report, the JRS's ratio of actuarial assets to accrued liability is 116%. If the assets were high enough to cover the amount necessary to pay all anticipated future benefits, in addition to those earned to date, this ratio would have to be closer to 130%.

The Office of Retirement Services informed the Senate Fiscal Agency of the amount that would be necessary to provide for the up-to-\$900 annual increases. In the first year, an estimated \$3.88 million would be necessary to cover a \$900 increase throughout the lifetimes of retired judges, and the cost would be one-time. The next time the trigger was hit, another one-time cost of \$3.88 million would be incurred. In future years, if the existing assets in the JRS and employee contributions were not enough to cover this increased base pension, the additional funds would come from the Court Fee Fund. As a result, the State would have to use additional GF/GP dollars for judicial salaries, meaning a reduction in GF/GP funding elsewhere in the State's budget.

Turning to the second purpose in the bill, it is estimated that only one person would be eligible to receive the 67% annual pension supplement detailed in proposed Section 514. It is further estimated that the pension adjustment provided would cost \$15,000 per year. However, whether the retirement rate otherwise charged to the judiciary would be affected based on this single adjustment would depend upon the value of the assets in the JRS and how much the system is "overfunded". Likely, since this would be an adjustment to only one judge's pension, the impact would be minimal, if any.

Under this legislation, a local fiscal impact would occur only if the obligations arising from the possible pension adjustments necessitated depositing into the JRS not only the approximately \$7.1 million from the Court Fee Fund, but also the \$2.2 million that goes to the Court Equity Fund.

Fiscal Analyst: Kathryn Summers-Coty

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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.