Legislative Analysis

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PUBLIC SCHOOL RETIREMENT REVISIONS

Senate Bill 1227 (H-9)
Sponsor: Sen. Jud Gilbert
House Committee: Oversight and Investigations
Senate Committee: Appropriations

Complete to 4-26-10

A SUMMARY OF SENATE BILL 1227 (H-9)

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 between June 15 and October 1, 2010. Retirees would have to apply between May 1 and June 1, 2010 and would have until June 25, 2010 to withdraw their application.

In addition, the bill would provide a 1.7% multiplier in the pension formula for an employee who retires between June 15 and July 1, 2010 and would provide a 1.6% multiplier for an employee who retires after July 1 but by October 1, 2010. Currently a member's pension calculation equals their final average compensation (FAC) multiplied by their years of service multiplied by 1.5%. This would increase a retiree's pension allowance by 6.7% at the 1.6% multiplier or by 13.3% at the 1.7% multiplier. The bill would cap the final average compensation to which the additional multiplier was applied at $114,000.

The bill would allow for a superintendent or chief administrator to request an extension to allow an employee to remain until July 1, 2011. An extension would require approval by the State Superintendent of Public Instruction.

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 October 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. Funds deposited in the

irrevocable trust could be used to pay for retirement health care benefits for retirees and their eligible dependents now or in the future. The bill would also determine and credit regular interest for employee contributions paid into the trust in the same manner as interest amounts for the Member Investment Plan under Section 33.

Public School Academies (PSAs) and Third-Party Contracts

The bill would remove the exemption of PSAs, as defined in the Revised School Code, from MPSERS. In addition the bill would amend the definition of public school employee for the purposes of this act to include persons working in a reporting unit, or employer, who are employed by a third party. This would require that reporting units pay the contribution rate on the wages of all persons working in a reporting unit even if they are employed by a third party, except for in certain limited circumstances. This would not include a PSA employee who receives retirement benefits under the Optional Retirement Act of 1967. The bill would also require that a retiree that worked for a reporting unit would have to reimburse the retirement system for the amount of the MPSERS contribution rate multiplied by their wages and would allow the retirement system to deduct the payment from their pension allowance.

Phased Retirement Option

The bill would also include an option for retirees under which the employee could retire and draw their pension while still working part-time. An employee would have to reduce the number of hours worked by 50% and work no more than 1,040 hours. The option could be renewed annually but could not exceed a total of 3 years. This option would have to be approved by the reporting unit.

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.

A complete fiscal impact of the retirement incentives above would require an actuarial analysis. In the absence of such an analysis, the preliminary estimates below are based on those provided by the State Budget Office and the Office of Retirement Services for the Executive proposed revisions and are adjusted for the House Amendments.

Retirement Incentives
Increasing the pension calculation multiplier from 1.5% to 1.7%, along with allowing employees to leave as long as they have a combined 80 in age and years of service credit could cost an estimated $4.3 billion. The costs would be distributed over the next 6 years, but would potentially be partially offset by an estimated $2.1 billion in savings from replacing fewer employees and due to the salary differential for new employees. However, the estimated cost increases due to the multiplier would be diminished to whatever extent employees retire after July 1 and qualify for a 1.6% multiplier rather than 1.7%. The estimated net cost of these proposals would be $2.1 billion paid from FY 2010-11 through FY 2015-16. 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 50% of eligible employees would retire under the bill's provisions, and that districts would replace 90%. To the extent that the bill would allow districts to avoid layoffs, the bill would also create an indeterminate amount of savings by decreasing unemployment costs.

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 approximately $300 million for FY 2010-11 and could total $3.0 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.

Public School Academies (PSAs) and Third-Party Contracts
Requiring employers to pay the MPSERS contribution rate on wages paid to persons working in the reporting unit but employed by a third party would have an indeterminate fiscal impact on MSPERS employers. The provision may increase costs for some employers that pay a significant portion of wages in contracted services, but could create savings statewide by increasing the funds paid to the pension system and potentially lowering retirement contribution rates. Additionally, requiring retirees who work on contract to reimburse the retirement system would increase funds paid to the pension

system and could potentially lower retirement contribution rates. 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. While the bill would create net savings in the first year, this is because of an actuarial lag such that the added costs of the retirement incentives are not borne by the MPSERS employers until the following five years. During that period, the incentives create a significant annual net cost, ranging from $60.7 million to $352.6 million. In years following FY 2015-16, the proposal would create an ongoing savings because of the added 3% employee contribution, assuming it is used to decrease employer contributions.

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.

Estimated Fiscal Impact of SB 1227 (H-9)
(in millions)

	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	**Cumulative 10 Year Total**
Increase Multiplier to 1.7%	$0.0	($380.0)	($380.0)	($380.0)	($380.0)	($380.0)	$0.0	$0.0	$0.0	$0.0	**($1,900.0)**
80 and out	$0.0	($272.6)	($272.6)	($272.6)	($272.6)	($272.6)	$0.0	$0.0	$0.0	$0.0	**($1,363.0)**
Increased Retiree Health Costs	($195.0)	($195.0)	($195.0)	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	**($585.0)**
80 and out health	($85.9)	($85.9)	($85.9)	($85.9)	($85.9)	$0.0	$0.0	$0.0	$0.0	$0.0	**($429.5)**
Years of Service 30yr Cap	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	**$0.0**
3% Employee Contribution	$300.0	$300.0	$300.0	$300.0	$300.0	$300.0	$300.0	$300.0	$300.0	$300.0	**$3,000.0**
Eliminate Retiree Dental/Vision	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	**$0.0**
Hybrid Plan for New Employees	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	**$0.0**
Replacement Savings	$716.0	$572.8	$429.6	$286.4	$143.2	$0.0	$0.0	$0.0	$0.0	$0.0	**$2,148.0**
GROSS SAVINGS/(COSTS)	**$735.1**	**($60.7)**	**($203.9)**	**($152.1)**	**($295.3)**	**($352.6)**	**$300.0**	**$300.0**	**$300.0**	**$300.0**	**$870.5**

Assumptions:

A complete fiscal analysis of the changes proposed above requires an actuarial analysis to determine savings/costs. In the absence of such an analysis, the preliminary estimates above are based on those provided by SBO/ORS for the Executive Proposed Revisions and are adjusted for the House amendments with the following assumptions:

1. Assumes 17,000 additional eligibles with 80 and out.
2. Assumes 50% participation of all eligible employees.
3. Tapers replacement savings down over 5 years to assume those retirements would have happened over the next 5 years regardless. Only counts savings directly attributable to the incentives.
4. Uses previous ORS Rule of 80 to calculate additional cost of added pension years and health care for a 30 and out.
5. Assumes all participating eligible employees leave prior to July 1 in order to receive a 1.7% multiplier. Costs would decrease to the extent that employees retire between July 1 and October 1 and receive a 1.6% multiplier.

Fiscal Impact:

While the bill would create savings in the first year, this is because of an actuarial lag such that the added costs of the retirement incentives are not borne by the MPSERS employers until years 2-6. During that period, the incentives create a significant annual net cost, ranging from $60.7 million to $352.6 million. In years following year 6, the proposal would create an ongoing savings because of the added 3% employee contribution, if the employee contribution is used to reduce the employer contribution as opposed to being saved to pay future retiree health care costs.