

MUNICIPAL RETIREMENT REVISIONS

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House Bill 5725 (H-2)
Sponsor: Rep. MacGregor

Senate Bill 1129 (H-1)
Sponsor: Sen. Colbeck

Committee: Appropriations
Complete to 9-25-12

A SUMMARY OF HOUSE BILL 5725 (H-1) AND SENATE BILL 1129 (H-1) AS REPORTED FROM COMMITTEE:

House Bill 5725 would amend the Municipal Employees Retirement Act of 1984 to specify that, by a majority vote of its government body, a municipality participating in the Municipal Employees Retirement System (MERS) could revoke its election to be governed by the provisions of the retirement system. A municipality could make such a revocation for all members in a retirement plan, or for any subset of members or any specific retirement program.

In order to revoke participation in a MERS retirement plan under the bill, a municipality would be required to do both of the following:

- Notify the Department of Treasury of its decision.
- Close eligibility for new hires from participating in the defined benefit (DB) retirement program.

The municipality could not revoke its participation in MERS unless the department determined it was in the fiscal interest of the municipality. The department would be required to notify the municipality in writing of its determination—within 90 days if the revocation related to a DB program and within 30 days if it related to a defined contribution (DC) program.

If the department determined that the revocation was not in the fiscal interest of the municipality, the municipality could request a reconsideration of the determination, subject to certain deadlines specified in the bill. The department's determination under such a request would not be subject to appeal, but the municipality could again seek to revoke its election to participate in MERS after at least 24 months had passed.

If the department determined that the revocation was not in the fiscal interest of the municipality, the bill states that MERS could not require a participating municipality to

participate in another retirement plan administered by the system as a condition of revoking its participation in an existing plan.

The bill would require a municipality revoking its participation in a MERS retirement plan to fund its contribution requirements for accrued financial benefits (i.e., the municipality's portion of the retirement plan's defined benefit unfunded accrued liability [UAL]), as required by the State Constitution.

The bill states that the amended act would not eliminate or diminish a member's vested retirement benefits earned before a municipality took the action authorized by the bill.

Finally, the bill would add provisions related to actuarially determining employer contributions, requiring the MERS board and the actuary to take into account the standards of practice of the Actuarial Standards Board of the American Academy of Actuaries, consistent with the Public Employee Retirement System Act. For a municipality that has closed DB program eligibility for new hires, the required contributions would include amortization payments to fund any UAL in accordance with the MERS board's amortization policy for closed divisions within an open participating municipality. MERS would be required to use the same amortization period for open and closed divisions.

Senate Bill 1129 (H-1) would amend the Revised Municipal Finance Act to allow, through December 31, 2014, a county, city, village, or township closing a DB retirement plan (completely or to new employees) and implementing a DC retirement plan, or a local unit that has already done so, to issue a municipal security to pay all or part of the costs of the UAL associated with the DB plan. (The term "local unit" is used in this document to refer to a county, city, village, or township.)

A local unit, through December 31, 2014, could similarly issue a municipal security to pay the costs of a health care UAL. The bill states that the funding of postemployment health care benefits by a local unit under the act does not constitute a contract to pay the benefits.

These actions would be open only to a local unit that has been assigned a credit rating of AA or higher by at least one nationally recognized credit agency and could be undertaken by ordinance or resolution of the municipality's governing body, without a vote of its electors.

The ability to issue the securities authorized under Senate Bill 1129 would be subject to the following provisions:

- The amount of taxes necessary to pay the principal and interest on the security, together with other taxes levied for the same year, could not exceed the limit authorized by law.
- A local unit issuing a security would be required to publish a notice of intent, make a comprehensive financial plan containing specified information (including,

in the case of borrowing for a health care UAL, a plan to mitigate the increase in health care costs) available to the public, and obtain approval from the state Department of Treasury.

- Borrowing proceeds could be used to pay the costs of issuance of the security. Proceeds from borrowing for a health care UAL would be required to be deposited in a health care trust fund, subject to certain requirements specified in the bill.
- A local unit issuing a security could not change the benefit structure of a DB plan if the plan is being partially closed, except that the local unit could reduce benefits for future years of service.
- A local unit issuing a security would be required to covenant with the holders of the security and the State of Michigan that it would not rescind whatever action it had taken to partially or completely close its DB plan.

Securities issued under the bill's provisions would be exempted from state and local taxation.

BACKGROUND INFORMATION:

MERS is an independent non-profit public organization that provides retirement plans that Michigan municipalities may adopt for their employees. Prior to the enactment of Public Act 220 of 1996, MERS was operated by the State of Michigan. According to MERS, approximately 750 municipalities—including cities, counties, hospitals, libraries, medical care facilities, road commissions, townships, villages, and other units of local government—participate in MERS, with more than 86,000 individual members and retirees.¹ As of September 30, 2010, net assets for MERS retirement plans totaled \$6.6 billion.²

FISCAL IMPACT:

The bills would have an indeterminate fiscal impact on local units of government currently participating in MERS or other DB or health care retirement plans.

House Bill 5725

Reportedly, municipalities are currently required to hold a local referendum to move employees out of MERS retirement plans under MERS plan documents. To the extent that House Bill 5725 resulted in more municipalities moving employees out of MERS by requiring only a vote of the governing body, financial savings could accrue to those municipalities, depending on the benefit levels and costs of the existing DB plan compared to the costs of the DC or other retirement plan into which employees were moved. (It is possible for a DC plan to have higher employer costs than a DB plan depending on benefit and employee contribution levels.) Moving from a DB plan to a DC plan eliminates risk for future benefits accrued under the DC system, but risk

¹ http://www.mersofmich.com/index.php?option=com_content&task=view&id=42&Itemid=176

² http://mersofmich.com/formfiles/popcafr_2010.pdf

associated with the DB system is not eliminated until a municipality no longer has any employees accruing benefits or retirees receiving benefits remaining in that system.

The bill's provisions regarding required contributions for a municipality's portion of the retirement plan UAL should ensure that MERS assets are sufficient to meet long-term benefit obligations. Generally, government accounting rules provide for accelerated amortization of UAL payments when a DB system is closed. There is a small risk that a municipality with no employees left in the system would become unable to pay its UAL costs for unforeseen reasons.

The bill would create an indeterminate amount of administrative costs for the Department of Treasury to make determinations regarding whether revoking participation in MERS was in the fiscal interest of a municipality.

Senate Bill 1129

To the extent eligible counties, cities, villages, or townships opted to issue securities to pay off the UAL, those local units would incur fixed debt obligations, as opposed to retirement system contributions for UAL costs which increase or decrease as investment returns and other factors built into actuarial assumptions fluctuate over time. (New UAL costs could arise over time, beyond those the local unit initially borrows for.) Generally, securities issued for this purpose are not exempt from federal taxation since the purpose of the borrowing is to take advantage of borrowing rates that are lower than assumed rates of returns for DB system investments. The amount of any savings (or costs) to local units borrowing under the bill's provisions would depend on the interest rate at which they could borrow funds relative to future retirement system investment returns.

The bill would create an indeterminate amount of administrative costs for the Department of Treasury to review and approve the issuance of securities allowed under its provisions over the next two years.

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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.