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BILL ANALYSIS

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House Bill 5355 (Substitute S-1 as reported by the Committee of the Whole)
Sponsor: Representative Thomas Albert
House Committee: Financial Liability Reform
Senate Committee: Education

CONTENT

The bill would amend the Michigan Public School Employees Retirement System (MPSERS) Act to change the calculation of the unfunded actuarial accrued liability (UAAL) contribution rate from a level-percent of payroll to a level-dollar, by reducing the assumed rate of payroll growth from 3.5% to 0% in 0.5% increments, beginning with the fiscal year (FY) 2018-19 valuation (which would have an impact on the State budget in FY 2021-22). In addition, the bill would require the UAAL contribution rate to be applied to payroll adjusted by the growth rate of payroll plus purchased services, instead of the current requirement that the rate be applied to payroll plus the growth in current operating expenditures, and would delay the implementation of this process until FY 2019-20.

Under current law, when there is an unfunded accrued liability in the retirement system (i.e., when dollars available in the retirement system are insufficient to fully fund all earned benefits if they had to be paid out in their entirety today), a contribution toward the UAAL is calculated. The UAAL is amortized like a mortgage: an end date is set and payments are calculated over the time period, with the goal to pay off the UAAL by that end date.

Under current law, the end date is FY 2037-38, and payments toward the "mortgage" are calculated as a level percentage of payroll, with payroll assumed to grow 3.5% per year. The effect is that a level percent of payroll applied to an assumed growing payroll base would lead to larger payments in the future. However, actual payroll growth has not achieved 3.5%, and in fact, has been negative in a number of recent years. This has led to a "shorting" of actual dollars contributed toward the UAAL, with the shortages being collected over the next five years with interest in order to keep the system whole.

The bill would change the method of paying toward the UAAL from a level percentage of payroll to a level dollar. The bill would require the assumed growth in payroll to be reduced by 50 basis points (0.50) each year, beginning with the FY 2018-19 valuation, which would affect the FY 2021-22 State budget and local employer contribution rates. The assumption about growth in payroll would decline to 3.0% in FY 2021-22, 2.5% in FY 2022-23, and so on, until a 0% growth in payroll was assumed beginning in FY 2027-28. At that time, the effect would be a level-dollar contribution toward the UAAL, meaning that each year's payment toward the "mortgage" would be approximately the same as the previous year's.

Also, the bill would allow the Office of Retirement Services (ORS) to reduce the assumed growth in payroll by 25 basis points (0.25%) instead of 50, if the cost of reducing payroll growth by 50 basis points exceeded 7% of the total cost of the prior-year UAAL payment. Further, the bill would allow ORS and the MPSERS retirement board to reduce the rate by any number of additional basis points, beginning in FY 2021-22.

The bill also would change the base on which the UAAL contribution rate is applied, from payroll adjusted by the growth in the prior year's current operating expenditures (COE) to payroll adjusted by the growth in the prior year's payroll plus purchased services; the change would be first applied in FY 2019-20. The bill would define "payroll plus purchased services" as the total of salaries, professional and technical services, client/pupil transportation and repairs and maintenance services expenditures including the charges incurred in the general, special education, and vocational education funds. This change would avoid the circular nature of including State payments for MPSERS in COE.

MCL 38.1341

FISCAL IMPACT

Table 1 shows the estimated UAAL contributions in millions of dollars as estimated under the bill (column 1), and also under current law with a 3.5% assumed payroll growth (PG) but actual payroll growth of 1.5% annually (column 2). The table further shows the estimated contributions if there were no change to level dollar, but payroll was assumed to grow, and actually grew, at 1.5% annually (column 4). As shown, there would be additional costs in the early years under the bill compared to current law with low actual payroll growth, but savings of $2.9 billion over 20 years due to frontloading contributions. Compared to keeping current law level-percent, but lowering the assumed growth in payroll to 1.5%, the long-term savings are estimated at $262.6 million.

Table 1

Estimated UAAL Contributions in Millions					
	(1)	**(2)**	**(3)**	**(4)**	**(5)**
Fiscal Year	**HB 5355 (S-1): Actual Payroll Growth (PG) =1.5%**	**Current Law Where Actual PG = 1.5% but PG Assumption = 3.5%**	**Difference between Contributions under HB 5355 and Current Law**	**Current Law Level Percent, but with Assumed and Actual Payroll Growth of 1.5%**	**Difference between Contributions under HB 5355 and CL with 1.5% PG**
2019	$2,900.5	$2,900.5	$0.0	$2,900.5	$0.0
2020	2,943.9	2,943.9	0.0	2,943.9	0.0
2021	3,003.4	3,003.4	0.0	3,407.1	(403.66)
2022	3,159.9	3,064.8	95.1	3,458.1	(298.20)
2023	3,343.2	3,127.8	215.4	3,510.3	(167.08)
2024	3,528.0	3,191.6	336.4	3,562.8	(34.84)
2025	3,698.4	3,257.5	440.9	3,616.1	82.25
2026	3,851.2	3,325.0	526.2	3,670.6	180.61
2027	3,982.6	3,406.2	576.4	3,725.4	257.18
2028	4,089.4	3,545.4	544.0	3,781.4	308.02
2029	4,089.8	3,692.9	396.9	3,838.1	251.71
2030	4,089.3	3,847.1	242.2	3,895.6	193.74
2031	4,089.1	4,010.6	78.5	3,954.2	134.93
2032	4,088.9	4,187.6	(98.70)	4,013.5	75.37
2033	4,088.7	4,376.4	(287.70)	4,073.6	15.05
2034	4,090.1	4,582.2	(492.10)	4,134.9	(44.80)
2035	4,089.2	4,810.7	(721.50)	4,196.9	(107.71)
2036	4,089.6	5,074.2	(984.60)	4,259.7	(170.07)
2037	4,088.0	5,397.3	(1,309.30)	4,323.6	(235.57)
2038	4,089.1	6,528.9	(2,439.80)	4,388.6	(299.51)
TOTAL	**$75,392.3**	**$78,274.0**	**$(2,881.7)**	**$75,654.9**	**$(262.6)**
Source: Office of Retirement Services					

Not shown in the table are estimates if payroll actually grew at the currently-assumed 3.5% annually; in that case, keeping the level percent of payroll would be more cost effective than changing to a level dollar amortization calculation. As long as the UAAL contribution rate exceeds 20.96% of payroll, these additional costs in the early years will be borne by the School Aid Fund due to the MPSERS rate cap on UAAL contributions.

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