

Legislative Analysis



AMEND RETIREMENT PLAN OPTIONS FOR NEWLY QUALIFIED MPSERS PARTICIPANTS

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<http://www.house.mi.gov/hfa>

House Bill 5021 as reported from committee
Sponsor: Rep. Matt Koleszar
Committee: Education
Revised 11-21-23

Analysis available at
<http://www.legislature.mi.gov>

(Enacted as Public Act 250 of 2023)

SUMMARY:

House Bill 5021 would amend the Public School Employees Retirement Act to change the default retirement plan for newly qualified participants. There are presently two options, *Tier 1* and *Tier 2*.

Tier 1 means the retirement plan available to a member under the act.

Tier 2 means the state's 457 plan established under section 457 of the federal Internal Revenue Code for elective employee contributions and the state's 401(k) plan established under section 401(k) of the Internal Revenue Code for employer contributions.

Under current law, if an individual does not make an election regarding their retirement plan during the election period, they are defaulted to participating in Tier 2 only. Individuals who elect to participate in Tier 1 are also part of Tier 2. The bill would change this so that only those who first became qualified participants in the state retirement plan from February 1, 2018,¹ through June 30, 2024, would have Tier 2 as their default election. Beginning July 1, 2024, individuals would default to being Tier 1 participants if they do not make an election within the election period, while also being a qualified participant in Tier 2. That individual would also be eligible to accrue any service credit or qualify for any retirement allowance under Tier 1 under the terms established in section 81c of the act.²

Generally speaking, Tier 1 is a defined benefit plan, and Tier 2 refers to a defined contribution plan, with both tiers part of the Michigan Public School Employees Retirement System (MPSERS). An individual who first worked on or after February 1, 2018, and elected Tier 1 is in the "Pension Plus 2 plan."

The date an individual was first hired into an eligible position with a participating employer determines which defined benefit plan they are part of, if they elected to participate in Tier 1. According to the Office of Retirement Services:

The Pension Plus 2 plan combines a defined benefit (DB) or pension component and a DC [direct contribution] or savings component. It requires member and employer contributions toward both the DB and DC components, although member contributions to the DC component may be reduced to 0.0%. With the Pension Plus 2 plan, both employer and member DB contribution rates may change each fiscal year. The DB contribution rate is split evenly between the employer and the member. DC

¹ This date reflects changes to retirement plan elections made by [Public Act 92 of 2017](#)

² <http://legislature.mi.gov/doc.aspx?mcl-38-1381c>

contribution rates may change based on deduction percentage changes initiated by the member through Voya.³

MCL 38.1381d

BACKGROUND AND BRIEF DISCUSSION:

State law provides for a 75-day window for new hires in participating MPSERS units to decide if they want to go into the Pension Plus 2 plan or a 401(k) for their retirement plan. This window opens on the date an individual is hired into a reporting unit, even if they have not received formal notification from ORS.

If no election is made by the end of those 75 days, individuals are signed up for the 401(k) plan by default and forgo eligibility for entering the pension plan. While both forms of retirement plan allow individuals to withdraw and move their contributions if they leave a MPSERS unit prior to being fully vested, it is disadvantageous to do so. In the pension system, an individual must work for 10 years to become fully vested, while the 401(k) plan allows individuals to keep 50% of employer contributions after two years, 75% after three years, and 100% of employer contributions after four years.

Supporters of shifting the default option from 401(k) to pension say it offers more flexibility to the educator later on, as it is possible to start with a pension and transition to a 401(k), whereas the opposite cannot occur. Because approximately 58% of new hires fail to make an election, defaulting them into the pension plan preserves maximum flexibility to each person to decide later they wish to change their plan.

Opponents of the change say that because the pension plan takes longer to be fully vested, defaulting new hires (most of whom are recent college graduates) restricts their ability to keep employer contributions in their retirement plan if they leave because of the longer time frame.

FISCAL IMPACT:

House Bill 5021 would have an indeterminate fiscal impact on the state and would increase costs for local school districts, intermediate school districts (ISDs), public school academies (PSAs), and community colleges because it is assumed that more employees would participate in the Pension Plus 2 hybrid plan due to that plan's becoming the default option under the bill. The magnitude of these impacts would depend on the extent to which future employees elect or default into the Pension Plus 2 plan instead of the defined contribution plan.

Since 2018, according to the Office of Retirement Services, 25% of new employees have elected the Pension Plus 2 hybrid plan, 17% have elected the defined contribution plan, and 58% have failed to elect into a plan and have therefore defaulted into the defined contribution plan. By revising the default plan, the bill would increase the percentage of new employees that participate in the Pension Plus 2 hybrid plan and reduce the percentage that participate in the defined contribution plan. It is possible that some of the employees who failed to elect a plan did so because they wanted the defined contribution plan; therefore, the extent to which the bill would impact these percentages is unknown.

³ <https://www.michigan.gov/psru/reporting-resources/reporting-instruction-manual/6-member-benefit-plans-and-contributions/6-03-03-pension-plus-and-pension-plus-2-plans>

The bill could reduce costs to the state under section 147e of the School Aid Act, which provides \$90.4 million to offset certain costs to employers for both the Pension Plus 2 hybrid plan and the defined contribution plan. According to the Office of Retirement Services, each \$1 in payroll that shifts from the defined contribution plan to the Pension Plus 2 hybrid plan would save the state \$0.0117 in section 147e.

The bill could increase normal costs for local units because the net normal cost percentage of payroll for employers under the Pension Plus 2 plan slightly exceeds normal cost percentage under the defined contribution plan. It is estimated that for each \$1 in payroll that shifts from the DC plan to the PP2 hybrid plan the local unit would realize a cost increase of \$0.0137.

Lastly, to the extent that Pension Plus 2 participation is increased, the bill could result in the state and local units taking on additional financial risk, which would lead to increased costs in the long term if the Pension Plus 2 hybrid plan were to develop an unfunded actuarial accrued liability (UAAL) at any point in the future. As of the FY 2022 valuation, the Pension Plus 2 plan is 105.9% funded. Any UAAL costs would be shared equally by the employer and employee under the statute. To the extent that any UAAL was subject to the statutorily imposed cap of 20.96% of payroll, the cost beyond 20.96% would be borne by the state.

POSITIONS:

Representatives of the following entities testified in support of the bill (9-26-23):

- Office of Retirement Services
- Coalition for Secure Retirement

The following entities indicated support for the bill:

- Department of Education (9-26-23)
- Michigan Education Association (10-3-23)
- Michigan Association of Retired School Personnel (9-26-23)
- Wayne County Regional Educational Service Agency (9-26-23)
- American Federation of Teachers – Michigan (9-26-23)

The following entities indicated opposition to the bill (10-3-23):

- Great Lakes Education Project Education Fund
- Mackinac Center for Public Policy

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■ This analysis was prepared by nonpartisan House Fiscal Agency staff for use by House members in their deliberations and does not constitute an official statement of legislative intent.