Legislative Analysis

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ALLOW PUBLIC SCHOOL EMPLOYEES AND STATE EMPLOYEES TO JOIN PENSION PLAN

House Bill 6060 as introduced
Sponsor: Rep. Matt Koleszar

House Bill 6061 as introduced
Sponsor: Rep. Regina Weiss

Committee: Labor
Complete to 12-12-24

SUMMARY:

Together, House Bills 6060 and 6061 would amend the Public School Employees Retirement Act and the State Employees' Retirement Act to allow public school employees and certain state employees, respectively, to join a defined benefit pension plan.

House Bill 6060 would amend the Public School Employees Retirement Act to allow newly hired employees and current employees to opt in to the act's "Tier 1" defined benefit (DB) retirement plan.

The Public School Employees Retirement Act establishes and governs the Michigan Public School Employees Retirement System (MPSERS), the retirement system for Michigan's public school teachers and other public school employees. MPSERS consists of two options, Tier 1 and Tier 2, with hybrid plans available.

Generally speaking, Tier 1 is a defined benefit plan, and Tier 2 is a defined contribution (DC) plan. An employee's hire date determines which retirement plans they are eligible for (see **Background**, below). New hires default to being members in the Pension Plus 2 plan, meaning they are both Tier 1 members and Tier 2 qualified participants, if they do not choose otherwise within the 75 days following their employment. Traditional Tier 1 pension plans without a DC component have been closed to new employees since July 1, 2010.

New hires
Under House Bill 6060, MSPERS would have to allow each individual who first becomes a Tier 2 qualified participant and is hired after September 30, 2025, to elect to become a qualified participant in Tier 2, a member of Tier 1, or both a qualified participant in Tier 2 and a member of Tier 1.[1] MPSERS would have to determine a method of accepting elections between the date the individual begins employment and the 75th day after the individual's first payroll date.

MPSERS would have to provide a form on which eligible individuals could make an election, which would have to be accompanied by a description of the benefit options and include an acknowledgment that the individual has received the description of the benefit options.

[1] An individual who elects to be a qualified participant in Tier 2 and not a member of Tier 1 would not be included under the Public School Employees Retirement Act's definition of ***member***.

Pension opt-in for current employees

Between January 1, 2025, and April 1, 2025, each individual who is a qualified participant as of December 31, 2024, could make a written election to terminate their status as a qualified participant in Tier 2 and become a member in the Tier 1 defined benefit plan. An individual who does not elect to join Tier 1 would continue to be a qualified participant in the Tier 2 DC plan.

An election would be irrevocable, and an individual who files the written election would become a member of Tier 1 on April 1, 2025. The Michigan Department of Technology, Management, and Budget (DTMB) would have to determine the method by which an individual would make a written election, in consultation with MPSERS' actuary and the MPSERS Retirement Board.

If the individual is married at the time of the election, the election generally would not be effective unless signed by the individual's spouse. (The MPSERS Retirement Board could waive this requirement if the spouse's signature cannot be obtained due to extenuating circumstances.)

Elections would be subject to the Eligible Domestic Relations Order Act.

A member who elects to become a member of Tier 1 could purchase up to five years of service credit in a manner determined by the retirement system.

The service credit for a qualified participant who elects to become a member of Tier 1 could not be used to satisfy the minimum number of years of credit required to receive a retirement allowance under the act or to calculate the individual's retirement allowance.

If DTMB receives notification from the Internal Revenue Service that any of these provisions will cause MPSERS to be disqualified for tax purposes under the Internal Revenue Code, then those provisions would not apply.

Final average compensation

Retirement benefits for DB plan members are based on the member's final average compensation (FAC) and years of service. Under the Public School Employees Retirement Act, FAC is calculated based on the member's total compensation earned within the averaging period in which the aggregate amount of compensation was highest, divided by the service credit accrued during that period. Currently, the averaging period is 36 consecutive calendar months for a DB plan member hired before July 1, 2010, and 60 consecutive calendar months for a MPSERS member hired on or after July 1, 2010.[2]

Under House Bill 6060, the ***averaging period*** for an individual who first became a member on or after October 1, 2025, would be 36 calendar months.

[2] If the member has less than one year of credited service in the averaging period, the number of consecutive calendar months in the averaging period must be increased to the lowest number of consecutive calendar months that contains one year of service. The bill would not amend this provision.

Health care match

Generally speaking, the act requires employers to match employee Tier 2 contributions, up to 2%, for health care costs for individuals hired on or after September 4, 2012, or current employees who elected to opt into the 2% match. MPSERS must also calculate an amount to be credited to a Tier 2 account for a member who opts in that is equal to their 3% contributions toward retirement health care.[3] Employees additionally receive a lump sum deposited into a Health Reimbursement Account upon termination of employment equal to $1,000 for an employee who terminates employment prior to reaching age 60 with ten years of service or $2,000 for an employee who terminates employment after reaching age 60 with ten years of service.

Under House Bill 6060, these provisions would no longer apply after the bill takes effect.

Normal cost contributions

Finally, a member of the Pension Plus 2 plan would no longer be required to contribute their 50% share of normal cost contributions to the member investment plan.

MCL 38.1304 et al. (amended); MCL 138.1369h et al. (proposed)

House Bill 6061 would amend the State Employees' Retirement Act to automatically enroll newly hired employees in the act's "Tier 1" defined benefit (DB) retirement plan and to allow current employees to opt in to the DB plan.

The State Employees' Retirement Act establishes and governs the State Employees' Retirement System (SERS), the retirement system for employees of the Michigan Civil Service Commission, appointed executive officials, and employees of the legislature and judiciary. SERS is administered by the Office of Retirement Services and consists of two plans: a defined benefit pension plan (***Tier 1***) and a 401(k)-style defined contribution plan (***Tier 2***), with hybrid options available for certain employees (see **Background**, below). Members in the defined benefit (DB) plan become eligible to receive a monthly pension benefit when they meet certain age and service requirements, at an amount based on their final average compensation (FAC) and years of service. The DB plan closed to all new hires on March 31, 1997, and all new public employees are now automatically enrolled in the Tier 2 defined contribution SERS plan.

> ***Tier 1*** currently means the retirement plan available to an individual hired before March 31, 1997, who does not elect to become a qualified participant of Tier 2.
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> Under House Bill 6061, the term would additionally include both of the following:
> - The retirement plan available to an individual who was first hired between March 30, 1997, and the bill's effective date who elects to become a member of Tier 1 in accordance with the provisions of HB 6061.
> - An individual who was first employed and entered on the payroll on or after the date the bill takes effect.[4]

[3] 2024 PA 127 eliminated the 3% contribution toward retirement health care benefits now required of MPSERS employees, beginning in FY 2025-26: https://www.legislature.mi.gov/documents/2023-2024/billanalysis/House/pdf/2023-HLA-5803-5821B240.pdf.

[4] This provision presumably refers to a retirement plan available to these individuals.

Tier 2 means the retirement plan established under section 401(k) of the Internal Revenue Code that is available to qualified participants.

Pension opt-in for current employees

Between January 1, 2025, and March 1, 2025, each individual who is a Tier 2 qualified participant as of December 31, 2024, could make a written election to terminate their status as a qualified participant in Tier 2 and become a member in the Tier 1 defined benefit plan. An individual who does not elect to join Tier 1 would continue to be a qualified participant in the Tier 2 defined contribution plan.[5]

An election would be irrevocable, and an individual who files the written election would become a member of Tier 1 on June 1, 2025. The Michigan Department of Technology, Management, and Budget (DTMB) would have to determine the method by which an individual would make a written election, in consultation with SERS' actuary and the State of Michigan Retirement Board.

If the individual is married at the time of the election, the election generally would not be effective unless signed by the individual's spouse. (The retirement board could waive this requirement if the spouse's signature cannot be obtained due to extenuating circumstances.)

Elections would be subject to the Eligible Domestic Relations Order Act.

A member who elects to become a member of Tier 1 could purchase up to five years of service credit in a manner determined by SERS.

The service credit for a qualified participant who elects to become a member of Tier 1 could not be used to satisfy the minimum number of years of credit required to receive a retirement allowance under the act, to calculate the individual's retirement allowance, or to satisfy the minimum number of years of service credit required to receive retiree health benefits, as described below.

If DTMB receives notification from the Internal Revenue Service that any of these provisions will cause SERS to be disqualified for tax purposes under the Internal Revenue Code, then those provisions would not apply.

Retiree health care

Under current law, employees in the DC 401(k) plan who were hired between March 31, 1997, and January 1, 2012, vest into a graded premium health insurance benefit after completing ten years of service. Unless they elect to switch to an employer match of up to 2% of their compensation into a 401(k) or 457 plan, those employees earn an employer contribution of 3% of the insurance premium for the health care insurance provided by SERS for each year of service completed, up to a maximum of 90% after 30 years. Employees become eligible to elect health insurance coverage after they reach age 55 if they have 30 years of service or after they reach age 60 if they have ten years of service.

[5] The bill would specify that any employees hired between March 30, 1997, and the bill's effective date who did not elect to terminate participation in Tier 2 to join the DB plan are not eligible for membership in the Tier 1 plan.

These provisions do not apply to employees who were hired on or after January 1, 2012,[6] or employees hired before that date who choose an employer 401(k) or 457 match rather than retaining their health care insurance benefit. House Bill 6061 would eliminate these exemptions.

Employees receiving matching contributions in lieu of retiree health care have the option of purchasing a retiree health plan from the state's health plan if they immediately enroll upon retirement or separation from the state. HB 6061 would remove a provision that also grants this option to all employees hired after January 1, 2012.

MCL 38.1i et al. (amended); MCL 38.19k and 38.50b (proposed)

BACKGROUND:

Michigan Public School Employees Retirement System

2012 PA 300 required all employees in the Michigan Public School Employees Retirement System (MPSERS) who were hired prior to July 1, 2010, (when new employees began entering a new hybrid retirement plan) to make an election between three options:

- Increase their own retirement contributions to 4% for the Basic Plan and 7% for the Member Investment Plan (MIP) and maintain a 1.5% pension multiplier.
- Maintain current contribution rates but freeze existing benefits at a 1.5% multiplier and receive a 1.25% pension multiplier for future years of service.
- Freeze existing pension benefits and move into a defined contribution (DC), 401(k)-style plan with a flat 4% employer contribution for future service.

MPSERS has several different benefit plans depending on the hire date of employees:

- The Basic and Member Investment plans are traditional pension plans for employees hired before July 1, 2010.
- The hybrid Pension Plus Plan with both a pension and a DC benefit with employer match for employees hired between July 1, 2010, and February 1, 2018.[7]
- The hybrid Pension Plus 2 Plan with a pension and DC benefit, and a 50/50 contribution share between the employee and employer, for employees hired on or after February 1, 2018.[8] (The Pension Plus 2 Plan will close to new employees if the actuarial funded ratio falls below 85% for two consecutive years.)
- The Defined Contribution Plan, which has an automatic employer contribution of 4% of a participant's compensation and an additional 100% match of up to 3% of a participant's compensation for employees hired after September 4, 2012; employees who chose to transfer to the DC Plan in 2012; employees who were hired between February 1, 2018, and June 30, 2024, who did not choose the Pension Plus 2 Plan; or employees hired after July 1, 2024, who chose the DC plan.[9]
- Those hired since 2012 receive a matching contribution of up to 2% of compensation into a personal health care fund 401(k) plan.

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[6] Instead of the health care insurance benefit, new employees receive an employer match of up to 2% of their compensation into a 401(k) or 457 account for health care.

[7] https://www.legislature.mi.gov/documents/2009-2010/billanalysis/House/pdf/2009-HLA-1227-7.pdf

[8] See https://www.legislature.mi.gov/documents/2017-2018/billanalysis/House/pdf/2017-HLA-0401-A84AD1A8.pdf

[9] https://www.legislature.mi.gov/documents/2023-2024/billanalysis/House/pdf/2023-HLA-5021-7C034DC4.pdf

State Employees' Retirement System

2011 PA 264 required all employees in the State Employees' Retirement System (SERS) who were hired prior to December 31, 2011, to make an election between three options, effective April 1, 2012:[10]

- Remain in the DB pension plan and contribute 4% of their compensation until retirement.
- Freeze existing pension benefits and move into a defined contribution (DC), 401(k)-style plan with a flat 4% employer contribution for future service.
- Remain in the DB pension plan and contribute 4% of their compensation until attaining 30 years of service, then freeze existing pension benefits and move into a DC plan.

SERS has several different benefit plans depending on the hire date of employees:

- The Defined Benefit Classified Plan, a pension plan for employees who were hired before March 31, 1997.
- The Defined Benefit 30 Plan, a pension plan for employees who were hired before March 31, 1997, and elected to stay in the DB plan until attaining 30 years of service before switching to the DC plan for future service.
- The DB/DC Blend Plan, a hybrid plan with a pension and a DC benefit for employees hired before March 31, 1997, who elected to switch to the DC plan on April 1, 2012.
- The Defined Contribution Plan, which has an automatic employer contribution of 4% of a participant's compensation and an additional 100% match of up to 3% of a participant's compensation for employees who were hired on or after March 31, 1997, who transferred from a DB plan, or who were originally hired under the DB plan and returned to work after retirement.
- Those hired since 2012 receive a matching contribution of up to 2% of compensation into a personal health care fund 401(k) plan.

FISCAL IMPACT:

House Bills 6060 and 6061 would increase costs for employers (local school districts, intermediate school districts (ISDs), public school academies (PSAs), and community colleges in the case of HB 6060 and the state in the case of HB 6061) because it is assumed that more employees would participate in a pension, or pension/defined contribution hybrid (hybrid) under the provisions of the bill. Specifically, the bill would increase normal costs for employers because the net normal cost percentage of payroll for employers under the pension plan would presumably be higher than the hybrid which would presumably be higher than the defined contribution plan. Moreover, the bills would reauthorize retiree health care options for employees. The magnitude of the fiscal impact would depend on the extent to which future employees elect, or existing employees elect to convert, into a higher employer cost plan ranging from the pension plan at the high end to the defined contribution plan at the low end.

Additionally, to the extent that pension or hybrid plan participation is increased, the bill would result in the employer taking on additional financial risk, which would lead to increased costs in the long term if the pension or hybrid plan were to develop an unfunded actuarial accrued liability (UAAL) at any point in the future. That said, initially any conversion or new elections to the pension or hybrid plan should not affect the unfunded liabilities of MPSERS or SERS.

[10] https://www.legislature.mi.gov/documents/2011-2012/billanalysis/House/pdf/2011-HLA-4701-7.pdf

Unfunded liabilities could accrue in the future if actual experience failed to meet actuarial assumptions on factors like stock market returns and mortality rates.

Lastly, HB 6060 also includes a provision that would remove the normal cost 50/50 cost share requirement for members in the Pension Plus 2 plan. This would shift approximately $84.3 million of employee paid share to the employer based on the most recent MPSERS valuation.

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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.