SB 1040 H-3 House Floor Speech

Rick Olson, 6/13/2012

I rise to support this proposal to reform the MPSERS program. The changes proposed will put the program on a sound footing and ensure that the benefits offered by the program will in fact be able to be paid when they come due.

The first step in solving any problem is clearly defining it. Here the problems are:

1. **An Unfunded Liability totaling $45.2 Billion according to the last Comprehensive Annual Financial Report, and the CAFR expected soon will probably show that to be over $50 billion.**
2. **The contribution rates that employers pay into the system are projected to grow from 25.7% this year to 35% in just 5 years. This is compared with 12.17% in 2000 that we thought was outrageous when I became the business manager at Adrian Public Schools.**
3. **This is a tremendous burden on our schools which takes away money that could otherwise be used for educating the kids. This year, the total contributions into the system is about $1,635 per student, and if we do nothing, $2,552 in 2016-17.**

<u>Three Potential Solutions</u>

- **Increase employee contributions**
- **Decrease benefits**
- **Find additional money**

This proposed solution uses all three

This H-3 Proposal:

- **Increases employee contribution to 4% for Basic members and 7% for Member Investment Plan (MIP) members. This is not much of an increase from 6.4% for some employees who have been employed since July 1, 2008, while the increase will be a bit higher for longer term employees. Nonetheless, we cannot continue retirement plans that promised more than the state can afford to fund. At the same**

time, we should acknowledge the efforts of prior legislatures that have tightened the programs through the years. For example,

- **Hybrid retirement plan adopted in 2010 will be continued for new employees**
- **Same health care options for new employees as state employees**
- **Retirees would pay 20% of their health care, other than those who are age 65 and retired by 1/1/2013**
- **Total prefunding of health care – instead of the fiscally irresponsible "pay as you go" method of not paying for the benefits as they are earned**
    - **Partially fund the health care plan by continuing employee 3% contribution for health care, placed into individual accounts**
    - **Total prefunding of health care by $603 million additional funding, spread over 2013-2018**
        - **$470 million in health care escrow account**
        - **$133 million in 2011-12 MPSERS set aside**

<u>Goals of Reform</u>

- **Decrease the unfunded liability**
- **Lower future projected contribution rates**
- **Be reasonable with current retirees, current employees and offer reasonable fringe benefits to prospective employees**

This proposed solution achieves all three

<u>Fiscal Impact of H-1</u>

- **Unfunded liability reduced by $15.6 billion. This is a "game changer" and will send a strong message that Michigan is serious about addressing its fiscal challenges. In all fairness, note that this is comprised of about $5 billion of real savings and about another $10 billion of reductions to the unfunded liability due to changed actuarial assumptions allowed by the GASB rules because we are beginning to fully fund the health care portion of the program.**
- **Cap the employer contribution rate at 24.46%, assuming state payments continue to fully fund the health care program in future years. In the spirit of full**

disclosure, it must be noted that the cap on MPSERS contributions will have an Impact on future Per Pupil Foundation Grant amounts, dampening the potential future foundation grant increases.

We need to strike a balance between the effects on employees vs. making a difference long-term in reforming the system. I am well aware of the many good people I have worked with in our schools through the years. Again in the spirit of full disclosure, my wife is a vested member of the MPSERS system and I am a non-vested member.

Let's look at the Reasonableness to Employees Under the H-3 proposal:

- **The current employee contribution rates of 4% and 7% are on the high side when compared with other states, although comparing apples to apples is difficult**

- **When we compare the ratio of the burden placed on the employee versus the burden placed on the employer, the proposal's implied employee responsibility of 20% for Basic members and 33% for MIP members is less than the 43% borne by state employees', and yet the school employees do not bear the market risks of the defined contribution plan that state employees do.**

- **The employees (past, current and future) bear about $9 billion of the total $45.2 billion unfunded liability prior to changes, or 20% of the total burden, with the employer picking up the remainder. From these last two comparisons, you can see that any claim that we are "balancing this problem solely on the backs of the employees" is totally wrong.**

- **Retirees will pay more, but the "granny" provision retaining the 10% cost share for those who are age 65 and retired on January 1, 2013 will protect the aged.**

Conclusion: No one wants to pay more or receive less. Nonetheless, the $45-50 billion unfunded liability problem must be solved. On balance, this is a reasonable sharing of the burden.

Stranded Costs: "Stranded costs" are caused when an employee leaves the system as an employee with vested retirement or health care benefits, with unfunded liability associated with them, but with no requirement for either the employee or employer to fund that unfunded liability.

If the stranded cost problem is not addressed now, it is equivalent to sitting in a boat swamped with water, bailing furiously to get the water out of the boat, but failing to plug the hole in the bottom of the boat.

I am pleased that the proposal contains a solution to the stranded cost problem via the COE or "current operating expenditures" mechanism. Beginning in 2013-14 fiscal year for traditional public schools, their total MPSERS assessment will be split into two parts:

- **11.9% will be applied to Current Operating Expenditures and**
- **3.5% will be applied to payroll to cover the normal costs for the revised retirement and healthcare benefits. Together, this is equivalent to 24.46% of systemwide payroll.**

Other entities would pay 24.46% on payroll, because of their vastly different cost structures.

It is unfortunate that this reform proposal is complex, but this is just one of many complex issues we have been given the opportunity to address. Please join me in supporting this historic reform measure.