Michigan Public School Employees Retirement System:

Major Changes in Recent Years and More Changes to Come

The Michigan Public School Employees Retirement System (MPSERS) provides a defined benefit retirement system as well as health care benefits for members of the system upon their retirement. The MPSERS was originally created by Public Act 136 of 1947 and is currently operating under Public Act 300 of 1980, as amended. During 2011, the MPSERS had a total of 444,185 members:

- 192,435 retired employees receiving benefits
- 236,660 active member employees
- 15,090 inactive employees of MPSERS who will be eligible to draw retirement and health insurance benefits upon reaching a certain age (e.g., former school employees who vested in the MPSERS system but are now employed elsewhere)

There are currently 714 employer organizations that are members of MPSERS, including:

- 7 public universities[1]
- 28 community colleges
- Intermediate school districts
- Public K–12 school districts
- Certain public school academies
- Certain local library districts

At the seven public universities that are members of MPSERS, only those employees hired prior to January 1, 1996 are members of MPSERS. Public school academies have the option of joining MPSERS.

During the past few years there has been considerable discussion in Lansing concerning the financial viability of MPSERS. Concerns have been raised regarding the ongoing cost to employers of maintaining MPSERS. Under MPSERS, participating employers (community colleges, local K–12 school districts, etc.) are responsible for making the payments to support pension and health care benefits provided to employees covered by MPSERS. Factors such as a decline in the performance of investments of assets held by MPSERS, a decline in the number of active members of MPSERS, and increasing health care costs have pushed up the contribution rates that employers are required to contribute to MPSERS. These increased employer costs have led to substantial changes in the system during 2007 and 2010 as well as additional proposed changes in 2012.

On March 22, 2012, Senate Bill 1040 was introduced in the Michigan Senate; the primary sponsor is Sen. Roger Kahn. The bill seeks to decrease the retirement costs under MPSERS for employers through a combination of reducing benefits and increasing the share of retirement costs borne by active and retired members of MPSERS. In response to the introduction of this bill, the Coalition for Secure Retirement-Michigan has contracted with Public Sector Consultants (PSC) to research and write an analysis of Senate Bill 1040. The PSC analysis will also include a description of the current status of MPSERS, including the types of pension and health care benefits currently offered to members, a discussion of the current

[1] The seven public universities are: Central Michigan University, Eastern Michigan University, Ferris State University, Lake Superior State University, Michigan Technological University, Northern Michigan University, and Western Michigan University.

financial status of MPSERS, and a discussion of the impact of Senate Bill 1040 on both the financial status of MPSERS and on current and retired members of MPSERS.

TYPES OF MPSERS PENSION PLANS

There are currently three separate pension plans offered to MPSERS members. The type of plan under which a MPSERS employee is covered is dependent on that employee's date of original hire by a participating employer. The three types of pension plans are the Basic Plan, the Member Investment Plan, and the Hybrid Plan.

Basic Plan

Employees hired before January 1, 1990 are members of the Basic Plan. Under this plan members are eligible to retire at age 55 with at least 30 years of credited service under MPSERS. As an alternative, Basic Plan members are eligible to retire at age 60 with at least 10 years of credited service. The amount of the pension benefit for members under this plan is equal to years of service multiplied by 1.5% multiplied by the average compensation of the employee over 5 years. For example, a Basic Plan member who retires after 33 years of service with an average compensation level of $60,000 is entitled to an annual pension payment of $29,700 (33 x 1.5% x $60,000). The retiring member has numerous options involving the amount of the pension actually received, which are based primarily on decisions regarding survivor benefits.

Basic Plan members receive health care benefits on their retirement. The amount of the cost sharing between the employer and the retiree for these health care benefits is established by MPSERS and state law. Currently, Basic Plan members who are retired with a spouse are paying for 12.9% of the cost of their health care benefits with the remainder of the costs paid by MPSERS.

Members of this plan do not contribute a portion of their salary to support their future pension benefits, and prior to July 1, 2010, they likewise did not contribute to supporting their future retiree health care benefits. That changed on July 1, 2010, when Public Act 75 of 2010 required Basic Plan members to begin contributing 3% of their salary to help finance the cost of health care benefits for current retired members of MPSERS—a contribution that is being litigated in the Michigan courts.

Member Investment Plan

Employees hired after January 1, 1990 are members of the Member Investment Plan (MIP). Under MIP, members are eligible to retire at any age with at least 30 years of credited service under MPSERS. As an alternative, MIP members are eligible to retire at age 60 with at least 10 years of credited service. These members are also eligible to retire at age 60 with only 5 years of credited service if those 5 years of service are the 5 years prior to turning age 60. The amount of the pension benefit for MIP members is equal to years of service multiplied by 1.5 % multiplied by the average compensation of the employee over 3 years. For example, a MIP participant who retires after 33 years of service with an average compensation level of $60,000 is entitled to an annual pension payment of $29,700 (example calculation same as Basic Plan member above). The retiring member has numerous options involving the amount of the pension actually received, which are based primarily on decisions regarding survivor benefits. The amount of the MIP pension is increased by 3% per year into the future.

MIP members receive health care benefits on their retirement. The amount of the cost sharing between the employer and the retiree for these health care benefits is established by MPSERS and state law and is also dependent on the hiring date of the member. Current MIP members hired before July 1, 2008 and retired with a spouse are paying for 12.9% of the cost of their health care benefits with the remainder of the costs paid by MPSERS. MIP members hired after July 1, 2008 will earn a graded premium health care subsidy depending on the credited years of service. These employees will earn a 30% health care benefit after 10 years of credited service and will earn an additional 4% health care benefit for each additional year of service.

Members under this plan have contributed a portion of their salary to support their pension. Those members hired from January 1, 1990 to June 30, 2008 have contributed toward their pension at the following rates: 3.0% of the first $5,000 of annual salary, 3.6% from $5,001 to $15,000, and 4.3% on all salary above $15,000. Members hired after July 1, 2008 contribute toward their pension at the same rate as employees hired prior to that date, with the exception of contributing 6.4% on all salary above $15,000.

Prior to July 1, 2010, MIP members did not contribute a portion of their salary to support their future retiree health care benefits. As with Basic Plan members, Public Act 75 of 2010 required MIP members to begin contributing 3% of their salary to help finance the cost of health care benefits for current retired members of MPSERS.

Hybrid Plan

Employees hired after July 1, 2010 are members of a hybrid pension plan. This plan is a blending of a defined benefit pension plan and a defined contribution plan.

The defined benefit portion of the Hybrid Plan allows an employee to draw a pension beginning at age 60 with at least 10 years of credited service. The amount of the pension benefit for this type of member is equal to years of service multiplied by 1.5% multiplied by the average compensation over 5 years. The hybrid pension members will not receive any cost-of-living increases after the retirement date. The employees in the Hybrid Plan will be required to contribute $510 annually plus 6.4% of their salary above $15,000 annually to help fund their pension.

The defined contribution portion of this plan requires employees to contribute 2% of their annual salary. The employee has the option of opting out of this contribution. If the hybrid employee choses to make the 2% contribution to the defined contribution plan, the employer will match this with a 1% contribution. Any additional employee contribution to the defined contribution plan above 2% will not require an employer match unless agreed to under a local collective bargaining agreement. For all funds contributed in this portion of the hybrid plan, the employee is responsible for investing these funds from a menu of options (similar to a private 401(k) plan) and is eligible to draw these funds upon retirement based on Internal Revenue Service Code requirements.

Hybrid Plan members receive health care benefits on their retirement. The amount of the cost sharing between the employer and the retiree for these health care benefits is established by MPSERS and state law. Hybrid Plan members will earn a graded premium health care subsidy depending on the credited years of service. These employees will earn a 30% health care benefit after 10 years of credited service and will earn an additional 4% health care benefit for each additional year of service. Pursuant to provisions of Public Act 75 of 2010, Hybrid Plan members contribute 3% of their salary to help finance the cost of health care benefits for current retired members of MPSERS.

AVERAGE PENSIONS FOR RETIREES IN THE MPSERS

The average pension level for members of MPSERS is based on the average final earnings of the member along with the number of years of service credits earned while working. Based on the most recent Comprehensive Annual Financial Report of MPSERS, the total level of pension benefits paid during fiscal year (FY) 2010–11 equaled approximately $4 billion.[2] As shown in Exhibit 1, these pension benefits were paid to a total of 187,722 pension recipients, leading to an annual average MPSERS pension benefit of $21,189. While the average annual MPSERS pension is $21,189, 38.9% of all MPSERS pension benefits paid went to individuals with annual pensions of $12,000 per year or lower.

EXHIBIT 1. Average Annual Pension of Retired MPSERS Members

Annual pension	Number of retirees	Percentage of retirees
Under $4,800	34,413	18.3%
$4,801 to $9,600	28,272	15.1%
$9,601 to $14,400	19,250	10.3%
$14,401 to $19,200	15,846	8.4%
$19,201 to $21,600	7,478	4.0%
$21,601 to $24,000	7,761	4.1%
Over $24,000	74,702	39.8%
Total	**187,722**	

SOURCE: Comprehensive Annual Financial Report for the Fiscal Year Ended September 30, 2011, Michigan Public School Employees Retirement System, Office of Retirement Services, page 96.

FUNDING REQUIREMENTS OF PUBLIC PENSION SYSTEMS

The responsibility for funding the necessary payments to finance pension and health care benefits offered under MPSERS is shared among the employer members of MPSERS, the active employee members of MPSERS, and the retired members of MPSERS. While the State of Michigan, through the Office of Retirement Services, manages MPSERS, state government is not responsible for financing the system. The amount of funding that is the responsibility of the employer versus the active employee or the retired employee is established pursuant to state law. Under state law, any funding that is not the responsibility of the active employee or the retired employee becomes the financial responsibility of the employer member.

Federal Internal Revenue Service Code requires that all public pension systems fund **pension** benefits on a “pre-funded” – as opposed to “as-needed” or cash – basis. This means that the pension system should have an adequate amount of assets invested to cover

- the future projected costs of all of the **current retired** members of the pension system, **and**
- the future pension cost of all of the **active employee** members of the system (e.g., current workers who may someday become retirees).

If the value of the pension investments at any one time is not sufficient to pay these future pension costs, the pension system is said to have an “unfunded accrued liability” in its pension accounts. When an unfunded accrued liability exists, Michigan statute requires the retirement system to make additional payments into the pension system to eliminate the unfunded accrued liability over a 26-year period.

In contrast, the **health care** benefits provided to retirees under MPSERS are funded on a cash basis. This means the total amount of the health care expenditures of retired members are paid during the fiscal year

[2] Comprehensive Annual Financial Report for the Fiscal Year Ended September 30, 2011, Michigan Public School Employees Retirement System, Office of Retirement Services, page 92. Available: www.michigan.gov/documents/orsschools/Public_Schools-2011_CAFR_375806_7.pdf.

in which the health care costs were accrued. This is quite different from private pension systems, where health care benefits are paid on a pre-funded basis. The difference stems from the concern by the federal government that private companies could declare bankruptcy and leave health care benefits without adequate funding to cover future obligations—hence the pre-funding requirement for *private* pension plans. While bankruptcy in the public sector is possible, it is not as significant an issue in the public sector as in the private sector.

In public sector pensions, the pension system is required to report on the level of unfunded accrued liability in its health care accounts on an annual basis.

CURRENT FUNDING STATUS OF MPSERS

The most recent financial report which outlines the current funding status of MPSERS, the Comprehensive Annual Financial Report, is available is for the fiscal year ending September 30, 2011. This report contains the data regarding the current funding status of both pension and health care benefits provided under MPSERS, and Exhibit 2 provides a summary of this data.[3] With regard to pensions, the actuarial value of the invested pension assets, as of September 30, 2010, was $43.3 billion. The actuarially calculated value of the current and future pension obligations was $60.9 billion. This leaves an unfunded accrued liability of $17.6 billion. A comparison of the value of the pension assets with the future pension obligations leads to the conclusion that the MPSERS pensions are currently 71.1% funded.

EXHIBIT 2. Current Funding Status of Michigan MPSERS
Funding Status as of September 30, 2010 (millions of dollars)

Pension Accounts	
Actuarial Value of Pension Assets	$43,294
Actuarial Value of Pension Liabilities	$60,927
Unfunded Accrual Liability in Pension Accounts	–$17,633
Funded Ratio	71.1%
Health Care Accounts	
Actuarial Value of Assets	$999
Actuarial Value of Liabilities	$28,627
Unfunded Accrued Liability in Health Care Accounts	–$27,628
Funded Ratio	3.5%

SOURCE: Comprehensive Annual Financial Report for the Fiscal Year Ended September 30 ,2011, Michigan Public School Employees Retirement System, Office of Retirement Services, page 46.

The $17.6 billion of the unfunded accrued pension obligation will be eliminated by spreading this unfunded accrued liability over the next 26 years. Based on current actuarial assumptions, this unfunded accrued liability is then spread over the covered payroll of the existing members of MPSERS (see Exhibit 3). During the current fiscal year, FY 2011–12, a charge of 12.49% of payroll is made to each employer to cover this unfunded accrued pension liability. If all of the actuarial assumptions concerning both the future growth of assets and liabilities of the pension accounts are accurate, the payroll charge will eliminate the $17.6 billion of unfunded accrued pension liability. If the actuarial assumptions are incorrect, this percentage charge to payroll will be adjusted (either up or down) to reflect the actual change in pension assets and liabilities.

[3] Comprehensive Annual Financial Report for the Fiscal Year Ended September 30, 2011.

EXHIBIT 3. Recent History of MPSERS Funding Status of Pensions (millions of dollars)

Fiscal year ending September 30	Unfunded accrued pension liability	Percentage funding ratio for pensions	Payroll % charge for pension unfunded accrued liability
2001	1,375	96.5%	0.19%
2002	3,575	91.5	0.06
2003	6,043	86.5	0.68
2004	7,533	83.7	0.88
2005	9,995	79.3	2.01
2006	6,141	87.5	4.32
2007	5,771	88.7	5.70
2008	8,931	83.6	4.89
2009	11,982	78.9	4.56
2010	17,633	71.1	6.15

NOTE: While the data for the unfunded accrued liability for FY 2010-11 and FY 2011-12 is not available, the percentage charge for this liability to payroll is 8.42% in FY 2010-11 and 12.49% in FY 2011-12.
SOURCE: Comprehensive Annual Financial Report for the Fiscal Year Ending September 30, 2011, Michigan Public School Employees Retirement System, Office of Retirement Services.

In addition to showing funding status for pensions, Exhibit 2 also summarizes the funding status of health care benefits offered under MPSERS. As of September 30, 2010, the actuarial value of the assets available to back current and future MPSERS health care benefits is approximately $1 billion. This is the amount of the cash payments due for health care for the fiscal year for the current health care needs of MPSERS retired members. The actuarial calculated value of current and future health care costs was $28.6 billion. This leaves an unfunded accrued liability of $27.6 billion. As discussed above, in contrast to the $17.6 billion unfunded accrued liability in the MPSERS pension accounts, there is no current requirement under the Internal Revenue Service Code which mandates the elimination of the $27.6 billion unfunded accrued liability in health care. During the current fiscal year, FY 2011–12, the health care costs of MPSERS retirees are being paid on a cash basis. The total cost of providing health care for retired MPSERS members is 8.5% of the covered payroll of active MPSERS employees. This cost is funded by a 3.0% charge to the salary of active employees and a 5.5% charge to the total payroll of each employer member of MPSERS.

SENATE BILL 1040 PROPOSED CHANGES TO MPSERS

On March 22, 2012, Sen. Roger Kahn introduced Senate Bill 1040, with major elements summarized below:

Changes to Active Employees: The bill would make changes in the final level of compensation to be used to calculate pension payments. Specifically, the final level of compensation would not include merit pay, longevity pay, or any pay in the form of a tax sheltered annuity. The bill would also require that existing employees make a new 4% of salary contribution to MPSERS unless they accept reductions in the future level of pension payments earned on future years worked. In terms of future health care benefits, the bill would require that existing employees retiring on or after July 1, 2012 would not be eligible to receive retiree health care benefits until they reach the age of 60 years. In addition, existing employees would have the amount of the health care payment they receive based on a graded health care system as opposed to the current system.

Changes to Retired Employees: The bill would make one change to the benefits of MPSERS members already retired, by increasing the retired employee share of health care costs from the current level of 10% to a new level of 20% effective July 1, 2012.

Changes to Future MPSERS Members: The bill would eliminate retiree health care benefits for all employees hired after July 1, 2012 and replace these benefits with a 2% matching employer contribution into the 401(k) accounts of these future employees. Upon retirement, MPSERS will have no obligation for the health care cost of these employees.

A comprehensive analysis of Senate Bill 1040 has been prepared by the Senate Fiscal Agency and is available to the public at: http://legislature.mi.gov/doc.aspx?2012-SB-1040

COST IMPACT OF SENATE BILL 1040

The Office of Retirement Services has prepared estimates as to the impact of the passage of Senate Bill 1040 on MPSERS, and Exhibit 4 provides a summary of these estimates. The proposed changes to pensions contained in Senate Bill 1040 are projected to reduce employer contribution rates by 2.93%, resulting in a $1.7 billion reduction (9.6%) in the level of the unfunded accrued liability of pensions under MPSERS. The health care changes in the bill are estimated to reduce the unfunded accrued liability for retiree health care by a total of $7.5 billion. It should be noted that while the changes in Senate Bill 1040 will reduce the unfunded accrued liability of health care benefits, they are not structured to begin the pre-funding of these health care benefits.

EXHIBIT 4. Projected Fiscal Impact of Senate Bill 1040

Provision	Approximate Cost Avoidance
	Pensions
Higher Member Contribution Rates to Pensions	2.80% reduction in employer contribution rates and a $1.6 billion reduction in the pension unfunded accrued liability
Changes in the Definition of Final Average Compensation	0.13% reduction in employer contribution rates and a $55 million reduction in the pension unfunded accrued liability
	Health Care
Require 20% Health Care Premium for Retirees	$112 million savings to employer and a $3.3 billion reduction in the unfunded accrued liability for health care benefits
Change Retiree Health Care Benefit Age to 60 Years	$5 million savings to employers and $1.365 billion reduction in the unfunded accrued liability for health care benefits
Retroactive Graded Health Premium for Existing Employees	$5 million savings to employers and a $2.8 billion reduction in the unfunded accrued liability for health care benefits

SOURCE: Office of Retirement Services, March 29, 2012.

IMPORTANT ISSUES RAISED BY SENATE BILL 1040

As the legislature begins its debate on Senate Bill 1040, several important issues should be carefully and thoroughly discussed. These include potential constitutional problems, fairness to members of MPSERS, comparisons to recent changes enacted that affect members of the State Employees Retirement System, the impact of the proposed changes on the ability to recruit quality public school employees and the ability to maintain quality senior public school employees, and underlying causes of rising MPSERS costs.

Constitutional Issues

Senate Bill 1040, if enacted into law, will almost certainly be challenged legally on a constitutional basis. Sec. 24 of Article IX of the Constitution of the State of Michigan of 1963 reads as follows:

> *Sec. 24. The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby.*

Based on informal advice from the Office of the Attorney General, previous members of the legislature took this section to mean that while changes could be made in the pension benefits of employees yet to be hired, changes in pension benefits of existing employees could be challenged on a constitutional basis. As an example of this legal belief, when the State of Michigan enacted major changes to the State Employees Retirement System in 1997, the changes applied only to newly hired state employees. A similar pattern was followed with changes made to MPSERS in 2008 when the employee contribution rate to MPSERS for MIP members was increased for employees hired after July 1, 2008. This trend of applying pension changes only to newly hired members continued in 2010 when newly hired MPSERS members were required to join the Hybrid Plan.

The provisions of Senate Bill 1040 that require increased contribution rates by **existing active** members of the Basic Plan and MIP will almost certainly lead to litigation. The ultimate outcome of these types of proposed changes to the pensions of existing MPSERS members will likely be decided by the courts.

Fairness Issues

Senate Bill 1040 presents significant fairness issues that members of the legislature must consider as they debate this issue. On the one hand, the legislature has an obligation to consider the increases in the long-term unfunded accrued liability in MPSERS. Action should be taken to address this issue on behalf of the citizens of Michigan and the future long-term costs of MPSERS. On the other hand, the legislature has an obligation to be fair to the current and retired members of MPSERS. The fairness issue revolves around the fact that MPSERS members took jobs with the understanding that they would earn a certain level of pension and health care benefits upon their retirement. The changes in Senate Bill 1040 that impact retired and active MPSERS members will be viewed by many as a breach in the promises made to these employees. The legislature should also consider the fact that the nature of both private and public sector pension systems has significantly changed in recent years. Significant reforms have been made in both pensions and retiree health care benefits.

Such changes need to be considered in light of what is fair to the employee and what is in the necessary best interest of the state as a whole. The fairness debate should also include the recent changes that have already been made in MPSERS. These include the requirement that MPSERS members contribute 3% of their salary toward retiree health care and the recently enacted requirement that all active employees pay at least 20% of the total premium cost of their health care benefits. In addition, many MPSERS retirees must now pay the state income tax on their pensions for the first time.

This issue of fairness will be a very difficult one for members of the legislature, and it is further complicated by recent action of the legislature with regard to their own retirement benefits. When a decision was made in 2011 to eliminate retiree health care benefits for elected members of the legislature, members of the legislature decided to apply this change only to members who do not have six years of service in the legislature as of January 1, 2013.[4] This change protected 35 of the 38 members of the senate

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[4] Public Act 200 of 2011 amended the Legislative Retirement Act to eliminate health care coverage for legislators who do not have 6 years of legislative service as of January 1, 2013.

from being affected by the retirement health care changes. This decision on health care benefits for retired members of the legislature is not consistent with some of the health care changes proposed in Senate Bill 1040.

Ability to Recruit New Employees and Retain Existing Senior Employees

The passage of Senate Bill 1040 could affect the ability of local school districts to recruit high-quality new employees and to retain existing senior employees. The ability to recruit high-quality new employees is likely to be impacted by the elimination of retiree health care benefits and the replacement with a defined contribution retiree health care system for newly hired employees. Likewise, the ability to maintain high-quality senior school district employees will likely be affected by the change to require employees to be at least 60 years old to have health care coverage upon retirement. Many senior school district employees will likely be forced to retire earlier than they had planned in order to retire with health care benefits if they are under the age of 60. While it is impossible to measure the impact of Senate Bill 1040 on these issues, it is important to discuss these issues in the legislature.

Underlying Causes of Rising MPSERS Costs

Senate Bill 1040 as introduced addresses the issues of rising MPSERS costs to employers and the unfunded accrued liability by shifting costs to current and future retirees. While these actions reduce the current costs, the legislation does not address significant **causes** of the MPSERS cost increases such as:

- **Rising medical costs:** The state has taken advantage of opportunities to maximize federal subsidies (e.g., accessing the Medicare Advantage plan) and increased retiree cost-sharing. However, health care inflation nationwide has risen dramatically more than general inflation—so using these opportunities results in temporary improvements at best.
- **Failure to pre-fund health care benefits:** Although pre-funding contribution **amounts** have been calculated since 1999, those transfers have not been made. Therefore, any increase in retiree health care costs must be paid for through increased assessments on employers and employees. If Michigan chose to pre-fund retiree health coverage, at least some of any cost increase could be paid through investment returns—thereby reducing the annual increase paid by employers and employees.
- **Fewer workers per retiree:** As the population gets older—but also as local districts convert positions and services from MPSERS-covered employees to non-MPSERS-covered organizations or contracts—the ratio of active workers to retirees has declined. State policy changes, including incentives to encourage MPSERS members to retire early, have also increased employer costs by further decreasing the worker-to-retiree ratio.

Although the issue of rising medical costs is beyond the scope of Senate Bill 1040, Michigan could choose to address pre-funding health care costs and cost increases caused by state policy changes.

CONCLUSION

There is little doubt that MPSERS is facing significant financial challenges. These financial challenges are primarily a result of four separate factors:

1. The number of active employed members of MPSERS has declined by 23.8% from September 30, 2001 to September 30, 2010. This decline leads to a smaller active payroll to apply any of the current funding needs of MPSERS, driving up the percentage of payroll costs used to fund the system. This decline in the number of active employees is due to a decline in the number of students in the system coupled with a shifting of students to public school academies and the

effort across the state to privatize a number of school positions that were previously filled by members of MPSERS.

2. The number of retired members of MPSERS drawing benefits has increased by 43.6% from September 30, 2001 to September 30, 2010.
3. The actuarial value of the pension assets has only increased from $38.4 billion in FY 2000–01 to $43.3 billion in FY 2010–11. This is an increase of only $4.9 billion or 12.7% over ten years. This is far below the 8% annual increase in pension assets assumed in the actuarial calculations used in MPSERS.
4. The cost of providing health insurance coverage to retired members of MPSERS has increased substantially. From FY 2001–02 to FY 2010–11, the cost of providing health benefits to retired members of MPSERS has increased by 83.5%—caused primarily by increases in health care costs, but also caused by the absence of investment-returns from pre-funding these benefits.

These factors combined have resulted in significant increases in the total cost of funding MPSERS. During FY 2001–02, the average payroll charge for the employer cost of MPSERS for both pension and health benefits totaled 12.2% of payroll. During the current fiscal year, FY 2011–12, this percentage has increased to 24.5% – a doubling of the rate paid by the public employer over a ten-year period. According to MPSERS estimates, the employer costs of MPSERS will increase to 31.2% of payroll during FY 2013–14, which nearly triples the rate in 15 years.[5]

While there is little doubt that the cost to both the employer and the employee of maintaining MPSERS has increased in recent years, there is a question as to whether the current system is sustainable into the future. It is important to put the current financial status of MPSERS into context. While the unfunded accrued liability of the pension payments is currently $17.6 billion, only a decade ago the unfunded accrued liability of the pension payments was only $1.4 billion. The changes in the return on investments of MPSERS assets, caused primarily by a drop in the stock market along with a declining number of active members in MPSERS, has led to the large increase in the pension liability. The unfunded accrued liability for health care benefits is a different issue, and continuing to pay these benefits on a cash basis—and foregoing earnings from a pre-funded plan—remains an option for MPSERS. A major concern is the unfunded accrued pension liability, and Senate Bill 1040 attempts to address the future funding of MPSERS. The important point to consider is that there needs to be a balance between the future funding needs of MPSERS and fairness to the existing and retired employees of the system—and that some of the **causes** of MPSERS increases will remain unaffected.[6]

[5] State of Michigan, Office of Retirement Services. Available: http://www.michigan.gov/psru/0,2496,7-284-60462-273152--,00.html.
[6] Comprehensive Annual Financial Report, page 20.