SENATE FISCAL AGENCY

BRIEF BACKGROUND AND DESCRIPTION OF STATE SPENDING FOR THE MICHIGAN PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

The following briefly explains various Michigan Public School Employees' Retirement Systems (MPSERS) terms and funding items found in the School Aid, Community Colleges, and Higher Education budgets, and the chart on page 3 tracks historical spending on these areas related to MPSERS.

General Background:
Costs in MPSERS have been growing lately, as have costs in other retirement systems, notably because of the steep declines in 2008 and 2009 in the stock market. Most retirement systems, not just in Michigan, but across the nation, assume a rate of return similar to Michigan's assumed 8% rate (7% for the hybrid plan enacted for employees hired on or after July 1, 2010). When the stock markets lost billions in asset value in 2008 and 2009, it led to dramatic increases in the unfunded accrued liabilities of the systems and to declines in the funded ratios. Therefore, costs started growing for employers, and the Legislature and Governor responded with numerous reforms for MPSERS and the State Employees' Retirement System. Recent stock market gains have helped to somewhat stabilize overall costs.

MPSERS Cost Offset:
The MPSERS cost offset grants were actually first appropriated in the year BEFORE the MPSERS rate cap was put into statute. In FY 2011-12 (again, prior to the MPSERS rate cap), these grants were put into the School Aid budget simply to help districts with their growing retirement costs. In FY 2011-12, a total of $155.0 million was appropriated to help districts with their retirement costs, which equated to an average $100 per pupil reduction in costs, but the actual savings per district were based on the proportion each district's payroll represented out of the total MPSERS payroll. These grants were continued in FY 2012-13, again at $155.0 million, and, at the same time, the MPSERS rate cap was first put into place. In FY 2013-14, the grants were reduced to $100.0 million total (or average per-pupil savings of $66), and the $55.0 million cut from the grants was instead run through the foundation allowance formula (a different distribution than when based on payroll). The School Aid budgets for FY 2014-15, FY 2015-16, and FY 2016-17 continued the grants at $100.0 million.

MPSERS Reserve Fund:
The MPSERS Reserve Fund was created in the fiscal year (FY) 2011-12 budget with what was characterized as a one-time appropriation, totaling $133.0 million. It was simply School Aid Fund (SAF) dollars that were deposited into that reserve fund for future use. At the time, it was unknown if those dollars would be needed for future reforms, but they were placed there to be available for future appropriations.

In FY 2012-13, another $41.0 million was deposited into the fund, bringing the total State funding to $174.0 million. In addition, school retirees' 3% retiree health contributions required under PA 75 of 2010, are in this fund, but are currently the subject of litigation. In FY 2013-14, a withdrawal of $156.0 million was made from the State's $174.0 million (leaving $18.0 million), to help pay for the cost of the MPSERS rate cap. The FY 2014-15 budget spent the remaining $18.0 million in State funds, again to support the cost of the MPSERS rate cap. (The Reserve Fund appropriations are not really considered appropriations, because they were deposits or transfers from the SAF into the Reserve, for future spending.)

MPSERS Rate Cap:
Districts pay the cost of covered school employees' retirement by remitting a percentage of payroll to the State. That percentage is set by the Office of Retirement Services and is made up of two pieces – a 'normal' rate (to pay for each year of service accrued) and an 'unfunded accrued liability' rate (which makes yearly payments to reduce the shortfall in the system that is the difference between the System's assets versus the benefits that have been earned by employees). Paying down the shortfall can be thought of similar to a mortgage – the shortfall is amortized over a closed time period and yearly payments are made in order to fully fund the system by the targeted end date.

The MPSERS rate cap was established under PA 300 of 2012, with the first State costs appropriated in FY 2012-13. The MPSERS rate cap was put into place to cap the amount that districts pay toward the unfunded accrued liability (UAL) in MPSERS. The cost for schools to pay toward retirement was growing and a decision was made to freeze the portion paid toward the UAL at the FY 2011-12 level. Any UAL percentage above 20.96% is made up by the State. For FY 2016-17, the total UAL rate is estimated to be 32.66% of payroll, and the total State cost to pay the difference between the 32.66% total UAL rate and the 20.96% capped district rate is estimated at $982.8 million in the K-12 budget (of which $0.6 million is to support the cap for libraries), plus $73.2 million in the Community Colleges budget and $5.9 million in the Higher Education budget to pay for the equivalent of a rate cap, though a cap for participating universities has not (yet) been enacted. Again, for entities other than participating universities, this represents the 11.70% difference between the total UAL rate and the capped district rate.

MPSERS Extra Payment toward Unfunded Accrued Liabilities
The initial FY 2014-15 budget for School Aid included a new, one-time additional payment toward UAL in MPSERS of $108.0 million, which was reduced mid-year to $19.6 million. This payment can be viewed similar to an extra, one-time mortgage payment: it will reduce payments on the entire debt, but will not change annual payments in the short- or even medium-term.

Retiree Health Care Costs
Both the Community Colleges and Higher Education budgets have included appropriations to help offset growth in retiree health care costs. FY 2012-13 was the first year of assistance for health care in both budget areas, with Community Colleges receiving $1.7 million and Higher Education receiving $0.4 million. Community Colleges have continued to receive $1.7 million to assist with retiree health care costs in each of the last four budget cycles. Assistance to universities for FY 2016-17 is part of the $5.9 million for the proposed statutory rate cap mentioned above.

Cost Cap in Higher Education
As noted above, universities were not part of the rate cap on UAL enacted as part of PA 300 of 2012. However, in the FY 2014-15 budget, $4.0 million was appropriated to freeze the UAL payments universities were making at the FY 2013-14 level, $5.2 million was appropriated for FY 2015-16, and $5.9 million was appropriated for FY 2016-17 in anticipation of enactment of a statutory rate cap for universities.

MPSERS Appropriations by Budget Area

Dollars in Millions

K-12	Sec. 147c Rate Cap	Sec. 147a Cost Offset	Sec. 147d Add'l Liability	K-12 Total by Year
2012	$ -	$ 155.0	$ -	$ 155.0
2013	$ 160.5	$ 155.0	$ -	$ 315.5
2014	$ 405.5	$ 100.0	$ -	$ 505.5
2015	$ 676.4	$ 100.0	$ 19.6	$ 796.0
2016	$ 892.9	$ 100.0	$ -	$ 992.9
2017	$ 982.2	$ 100.0	$ -	$ 1,082.2

Community Colleges	Rate Cap	Retiree Heath	Total by Year
2012	$ -	$ -	$ -
2013	$ 12.5	$ 1.7	$ 14.2
2014	$ 31.4	$ 1.7	$ 33.1
2015	$ 52.3	$ 1.7	$ 54.0
2016	$ 69.5	$ 1.7	$ 71.2
2017	$ 73.2	$ 1.7	$ 74.9

Libraries	Rate Cap	n/a	Total by Year
2012	$ -	$ -	$ -
2013	$ 0.5	$ -	$ 0.5
2014	$ 1.3	$ -	$ 1.3
2015	$ 0.5	$ -	$ 0.5
2016	$ 0.6	$ -	$ 0.6
2017	$ 0.6	$ -	$ 0.6

Higher Education	Cost Cap	Retiree Health	Total by Year
2012	$ -	$ -	$ -
2013	$ -	$ 0.4	$ 0.4
2014	$ -	$ 2.4	$ 2.4
2015	$ 4.0	$ 2.4	$ 6.4
2016	$ 5.2	$ -	$ 5.2
2017	$ 5.9	$ -	$ 5.9

The Rate Cap column is the piece that is statutorily required to be paid, pursuant to PA 300 of 2012. It measures the amount required to be paid in toward unfunded accrued liabilities in excess of the 20.96% rate cap.

Cost Offset grants are provided to school districts only (not CCs or ISDs) to assist with overall MPSERS costs. These were in place prior to the rate cap of 2012.

The Sec. 147d $19.6 m additional liability payment is a new, one-time additional paydown toward unfunded accrued liabilities, similar to an extra mortgage payment.

Funding in CC and HE for Retiree Health is to help offset a portion of retiree health care costs. Cost Cap in Higher Education is to hold university costs flat at FY 14 levels for cost increases related to unfunded accrued liabilities.

FY 2011-12 and FY 2012-13 also saw deposits of SAF revenue into the MPSERS Reserve Fund, but since those were only transfers into the fund for support of future expenditure, and not direct expenditures themselves, they are not shown above.