Legislative Analysis

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MPSERS – NEW HYBRID AND NEW DC PLANS

House Bill 4647 (H-3) proposed Committee Substitute
Sponsor: Rep. Thomas Albert
Committee: Education Reform
Complete to 6-14-17

SUMMARY:

House Bill 4647 would amend the Public School Employees Retirement Act (the Act) to

- Reduce the assumed rate of return for the Basic and MIP pension plans from 7.5% to 7.25%.

- Reduce the assumed rate of return for the Hybrid plan from 7.0% to 6.5%.

- Replace the current optional DC plan, which offers a 50% employer match capped at 3% of an employee's compensation, with a DC plan that would mirror the current plan for state employees, with an automatic employer contribution equal to 4% of a participant's compensation plus a 100% matching contribution capped at an additional 3% of a participant's compensation.

FISCAL IMPACT:

The bill would have an indeterminate fiscal impact on the State and local units of government. The bill would increase the cost of MPSERS employer contributions for both applicable MPSERS employers and the state by an estimated $256 million in the first year of implementation, and the costs would increase annually as the number of employees in the new plans increased.

New DC Plan
For FY 2017-18, the maximum employer hybrid plan normal contribution rate is equal to 4.1% of a participant's compensation and the maximum normal rate for the optional DC plan is 3.0%. Under the bill, the maximum DC normal contribution rate would be 7.0%, including an automatic 4.0% contribution plus an additional matching contribution up to 3.0%.

The total increased normal costs are estimated at to be between $0 and $20.0 million for FY 2017-18, depending on how many people chose the DC plan. The costs would increase annually as the number of employees in the DC plan grows

Table 1: House Bill 4647 Fiscal Impact
(in Millions)

	(1)	(2)	(3)	(4)	
Fiscal Year	**Maximum Additional Annual Normal Cost of DC for New/ Converted Employees**	**Additional Annual Cost for MPSERS Hybrid to Move to 6.5% AROR**	**Additional Annual Cost for MPSERS to Move to 7.25% AROR**	**Total Additional Annual Cost for Other State Plans 7.25% AROR**	**Total Additional Annual Cost***
2018	$20	$38	$149	$49	**$256**
2019	$33	$16	$150	$50	**$249**
2020	$48	$21	$152	$51	**$272**
2021	$63	$26	$154	$52	**$295**
2022	$80	$31	$157	$53	**$321**
2023	$98	$36	$160	$54	**$348**
2024	$117	$41	$163	$55	**$376**
2025	$139	$47	$166	$56	**$408**
2026	$162	$53	$169	$57	**$441**
2027	$186	$59	$151	$58	**$454**
10-Yr Total	**$946**	**$368**	**$1,571**	**$535**	**$3,420**
	*Columns may not sum to total due to rounding.				

<u>Revised Investment Rate of Return Assumptions and Amortization Period</u>
Currently the MPSERS Board approved rate of return assumption is 7.5% for the pension plans other than the Hybrid plan and 7.0% for the Hybrid plan. Further decreasing the AROR for the pension plans to 7.25% would cost about $149 million in the first year and would grow annually along with increased payroll.

Reducing the Hybrid AROR from 7.0% to 6.5% would increase the normal rate from approximately 4.1% in total to 5.0% in total. The additional normal cost if all employees chose it would be between $0 and $16.2 million in year 1, depending on how many people choose it, and would grow annually along with payroll.

This would also create a UAAL in the system which if paid off in lump sum in the first year would cost $21.7 million. Reducing the assumed rate of return would include reducing the risk in the investment asset allocations to protect the asset pool to manage cash flow once benefit payments significantly exceed contributions. However, reducing the assumed rate of return also means reducing the assumed growth of investment income in the system, which decreases the actuarial estimate of long-term assets, and thereby increases the estimated UAAL. The increased UAAL increases the annual required contributions necessary to fund the system.

<u>Other Retirement Systems Impact</u>
MPSERS plan assets are pooled with the assets of other state retirement systems including the State Employees Retirement System (SERS), the State Police Retirement System (SPRS), and the Judges' Retirement System (JRS). SERS and JRS were closed in 1997 and replaced with a DC plan. SPRS has had a hybrid plan since 2012. The combined assets of all four plans are managed by the Department of Treasury, Bureau of Investments.

While the bill is silent regarding these other systems, reducing the assumed rate of return for MPSERS, for which the assets far outweigh those of the other systems combined, requires that Treasury revise the asset allocation of the entire asset pool. As described above, a reduction in the assumed rate of return reduces the long-term actuarial estimates of assets and increases the UAAL. The increased UAAL increases the annual required contributions into the state plans, which are funded as part of employee economics across all state departments in the annual appropriation process. The increased costs for the other state plans is estimated at $49 million in the first year and would increase annually throughout the remaining years in the amortization period, currently set to end as of September 30, 2036.

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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.