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Talk Rife Of Senate Moving New School Employees To 401k

Expectations are building that the Senate may take up legislation to move all public school employees hired after a certain date into a 401(k)-style defined contribution system before the end of the term.

Sen. Phil Pavlov, the sponsor of SB 102, which would make that move, said he could not confirm or deny any developments on what the Senate will do with the bill, which he introduced in February 2015. Mr. Pavlov has long advocated ending the current system that gives new teachers some pension benefit and some defined contribution benefit.

"I think our desire has always been we need a permanent fix to the unchecked liabilities that the retirement system is accumulating," Mr. Pavlov (R-St. Clair) told Gongwer News Service on Friday.

For years, legislative Republicans have been eyeing the unfunded liability issue with the defined benefits portion of Michigan Public School Employees Retirement System by pushing individuals into a defined contribution, 401(k)-style plan. In 2012, the Legislature created a hybrid system for new employees in MPSERS that provided some pension and some defined contribution benefits.

Also included in that law is the elimination of retiree health insurance for newly hired employees, which was replaced with a 401(k) or 457 plan that includes an employer match of up to 2 percent of compensation plus a lump sum deposit of either $1,000 or $2,000 upon termination of employment.

The 3 percent contribution public school employees currently make continued, but instead was redirected to prefund the retirement system. However, employees could decide to give up retiree health insurance coverage to end the 3 percent contribution and receive a 2 percent matching contribution like new employees would have.

Mr. Pavlov opposed the law then and encouraged a defined contribution system instead. The barrier at the time was the transition costs. A 2012 study determined that if public school employees were to be provided the same defined contribution plan as state employees receive - which Mr. Pavlov praised in his interview - the added cost would be $13.6 billion over 30 years. Critics of the existing system have questioned those numbers.

The report also said accounting rules would mean an additional $4.5 billion short-term cost to the state over the first 10 years if the hybrid plan were closed to new hires. Those rules would speed up the amortization period the state now has to pay down the system's unfunded liability, resulting in the added short-term burden (See Gongwer Michigan Report, November 21, 2012).

But as he maintained then, Mr. Pavlov thought the up-front costs were "a false argument."

"I think the transition costs were inflated in 2012," he said. "A retirement system costs what it costs, and we have an obligation to meet those (demands), and transition costs are always part of the conversation to keep this system in place."

He said his plan "simply closes the defined benefit retirement plan and converts all new hires to defined contribution. By doing that, you have zero future liabilities and you don't allow a system to get out of control like the MPSERS system has. This Legislature and governor have been firm in our commitment to retirees by shoring up that system, but a defined benefit system no longer fits the demands of a stable system."

As a point of reference, Mr. Pavlov said when he first entered office, the percentage of payroll to support the system was 13 percent, and today it's in the high 30s, he said.

STANDSTILL IN THE ADMINISTRATION: Kurt Weiss, spokesperson for the Department of Technology, Management and Budget, said the administration continues to support the hybrid system in place for MPSERS.

"That system has been very successful," Kerrie Vanden Bosch, director of retirement services, said in an interview. "The hybrid plan is 100 percent funded today, and it's one-third less risky than a defined benefit plan."

Ms. Vanden Bosch said currently, less than 20 percent of people are choosing a defined contribution plan. Everyone else is in the hybrid plan, she said, and costs have continued to remain low. They hybrid plan is about two-thirds the cost of a replacement defined contribution plan and provides better benefits as well, she said.

"I don't think most people understand (that) the liabilities on the MPSERS system are related to the legacy defined benefit plan, which has already been closed. The hybrid portion is 100 percent funded," Ms. Vanden Bosch said. "Nothing you do to new employees can reduce that legacy liability. If you were to close the hybrid plan, which again is 100 percent funded, that will not do anything to touch the existing defined benefit liability and will only increase it."

And that legacy liability is something Governor Rick Snyder has made a plan to pay down every year during the state budget, Mr. Weiss noted, until the liability is gone in 2038.

Mr. Pavlov said he expected that answer from the Office of Retirement Services, but that this is an opportunity to "change direction" by meeting obligations, paying commitments and still shielding taxpayers from paying this again.

While he doesn't set the agenda, Mr. Pavlov said he hopes for a "serious conversation about fixing it going forward" when the Legislature returns after the November election.

"There's a lot of support in our chamber to fix this. We'll continue to work on it and work on all options, particularly on addressing transition costs," he said. "It will only get more expensive year after year. We've been meeting those obligations above and beyond. We're funding health care, the long-term debt, but it's growing faster than you can throw money at it."

MEA WEIGHS IN: The Michigan Education Association is gearing up for a fight on pensions as well, as it warned members about a possible public pension challenge, especially after a speech in late September by Amway President Doug DeVos, who called restricting of government employee pensions the top goal of the conservative West Michigan Policy Forum.

"In his speech, DeVos said the West Michigan Policy Forum's vote to advocate moving public employees to a 401(k)-style retirement system 'sends a message to all of our elected officials. And we take these (votes) very seriously; we move them forward with all of our might,'" the MEA noted.

Indeed, Mr. Pavlov alluded to the possibility of more pension reform on the way as it relates to municipalities, though few details on who would lead that conversation or when it could happen were immediately known. Top Snyder aide John Walsh has restarted discussions on the topic, though that is expected to be more of a 2017 project (See Gongwer Michigan Report, September 16, 2016).

"There are only seven municipalities across the country that have a fully funded retirement systems. That should tell you there's a systemic problem here, and Michigan shouldn't be in that business anymore. But local communities will come to the Legislature with their problems as well.

"You can't outrun these liabilities. They grow so fast, grow so much debt. When municipalities come back to (refinance) it's not helping grow local economies," Mr. Pavlov said.

But Doug Pratt with the MEA said all of the pension reform talk - especially as it relates to MPSERS - is effectively a day late and a dollar short.

"This is a huge issue that impacts thousands of thousands of peoples' lives. Is it really something to handle in the last nine session days?" Mr. Pratt said. "It's a huge concern, especially because there have already been many changes ... those need time to have an impact. The hybrid system is fully funded. The unfunded liabilities are improving. Like any investment, it takes time to return from the economic downturn of 2008."

Mr. Pratt said about 45 percent of school employees receive a pension of less than $14,500 a year.

"That's not a rich pension by any stretch of the imagination. Why the DeVoses care about those people getting their $14,500 a year is beyond me," Mr. Pratt said. "The reforms made just a few years ago need time to be able to work."

LOOKING TO DETROIT: Former House Speaker Jase Bolger, whose consulting firm represents the West Michigan Policy Forum that sparked the MEA's concern on a possible public pension fight in lame duck, said that while the focus of the policy forum was local government pensions, he personally has talked to a couple different senators to say that they were right and he was wrong during the MPSERS debate four years ago.

"That was an evolution for me," Mr. Bolger said. "When it became clear was the Detroit bankruptcy. There were a couple of compromises - one was the Detroit presence on the oversight board and the other, the House had called for defined contribution within the settlement going forward."

Upon bankruptcy confirmation, Judge Steve Rhodes pointed to those two issues as potential problems, Mr. Bolger said.

"Defined contribution was the only way to make sure they didn't get back into the same mess again. Future politicians could ... make promises they couldn't keep. That was a moment that I frankly regretted we hadn't stuck to defined contribution and instead compromised to the (hybrid) definition we did, because I think Judge Rhodes was right - that's the only way to make sure the employees could control their pension."