



# Defined Benefit Plan Provisions

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# Agenda

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- How Defined Benefit Plans Work
- Overview of New Defined Benefit (DB) Plan Provision Options
- FAQs



# How Defined Benefit Plans Work

# Lifetime Benefit for Career Employees

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*Lifetime  
Retirement  
Benefit*



"Pension"



# Defined Benefit Formula

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The benefit formula is comprised of three components:

- Final Average Compensation
- Service Credit
- Benefit Multiplier

# Final Average Compensation



- Average of the highest consecutive wages
- Majority of divisions use a 3 or 5-year period
  - 3-year period (47%)
  - 5-year period (52%)
- The average compensation is \$54,889

# Service Credit



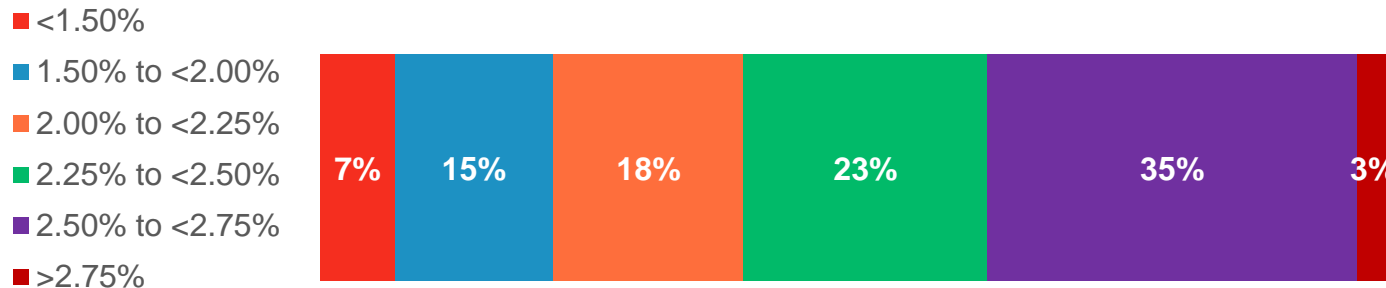
- Earned for each month of work that meets the employer's requirements
- To reach an 80% income replacement rate, a participant would need to work approximately 32 years (with a 2.5% multiplier)

# Benefit Multiplier



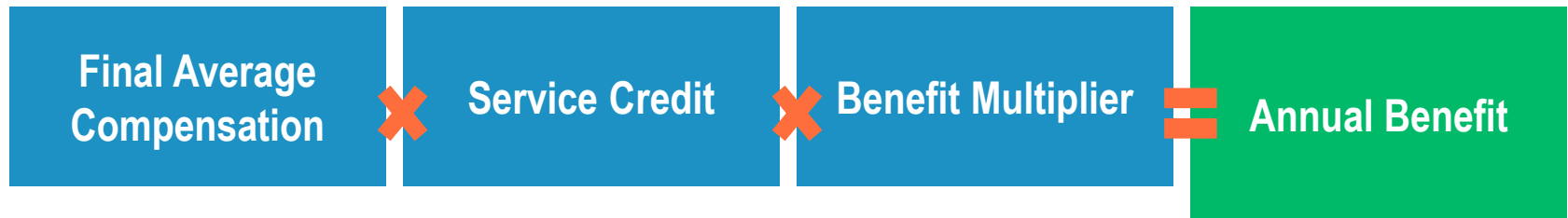
- Benefit multiplier is a specific percentage adopted by the employer
- About a third of divisions have a 2.5% multiplier
  - No new divisions are adopting this provision
  - Higher multiplier divisions may have opted out of Social Security

## PERCENTAGE OF DIVISIONS WITH CERTAIN MULTIPLIERS





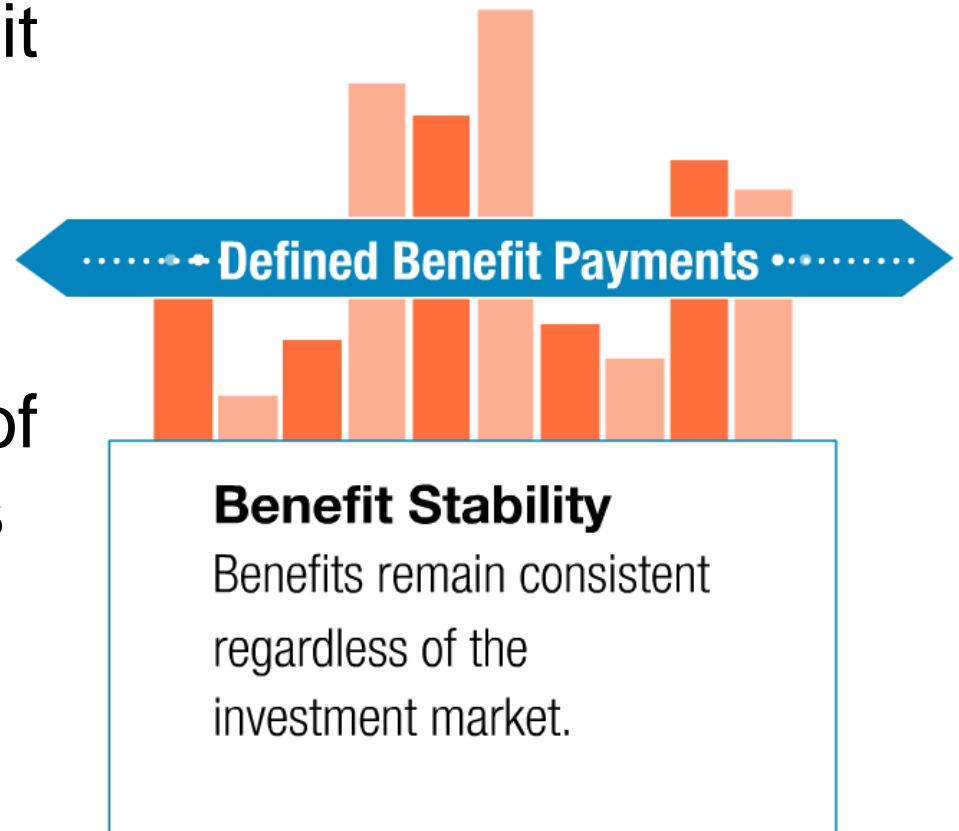
# Annual Benefit



- To be eligible to receive a benefit an employee must meet both age and service requirements (also called vesting)
  - Majority have an eligibility age of 60
  - 2/3 of divisions have a vesting period of 10 years
- Current benefits being paid out
  - 42,486 retirees and beneficiaries
  - Average annual benefit is \$22,339
  - Average age at retirement is 58
  - 1 in 5 open plans offers a cost of living adjustment

# Lifetime Benefit Stability

- The calculated benefit will not change with investment market fluctuations
- Retirement benefits of municipal employees are constitutionally protected





# DB Plan Provisions

# New DB Plan Provision Options

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- MERS is implementing some modifications to DB plan provision options
- **All employers will be asked to submit an updated Adoption Agreement Addendum to clarify provisions**
- While employers do not need to make any changes to their plans, if you do want to make changes they will become effective January 1, 2021 to prospective benefits only

# New Plan Provision Options

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- Plan Eligibility
- Service Credit Qualification
- Leaves of Absence
- Definition of Compensation

# Plan Eligibility Today

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- Plan eligibility **defines who participates** in the defined benefit plan
- Eligibility is based on a **defined “group” of employees**, and doesn't always follow a specific naming convention, which can lead to confusion
- Eligibility based on a defined “group” of employees and those who meet a “day of work definition” (hours in a month, days in a month) **are related**

# Plan Eligibility – 1/1/2021

- Employers will have the ability clarify the definition of eligibility by identifying which **classifications** of employees participant in the plan
- Employee classifications, including part-time employees can now be excluded

| Employee Classification  | Included                 | Excluded                 |
|--|--------------------------|--------------------------|
| <b>Temporary Employees:</b> Those who will work for the municipality fewer than [ ] months in total. | <input type="checkbox"/> | <input type="checkbox"/> |
| <b>Part-Time Employees:</b> Those who regularly work fewer than [ ] per [ ]                          | <input type="checkbox"/> | <input type="checkbox"/> |
| <b>Seasonal Employees:</b> Those who will work for the municipality from [ ] to [ ] only.            | <input type="checkbox"/> | <input type="checkbox"/> |
| <b>Voter-Elected Officials</b>   | <input type="checkbox"/> | <input type="checkbox"/> |
| <b>Appointed Officials:</b> An official appointed to a voter-elected office.                         | <input type="checkbox"/> | <input type="checkbox"/> |
| <b>Contract Employees</b>  | <input type="checkbox"/> | <input type="checkbox"/> |

# Day of Work Definition - Today

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- For the DB plan, how service credit is earned in a month is defined in days - known as “Day of Work”
- Over time, the information collected on this provision has varied from employer to employer
- It is assumed that employers are using the default unless they inform us differently



# Service Credit Qualification – 1/1/2021

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- The Day of Work definition will be replaced with **Service Credit Qualification**
- Service Credit Qualification will define the number of hours an eligible employee needs to work in a month to earn service credit
- There is **no default option**
- Creates a simple two-tiered approach to plan eligibility

**1**

Are you eligible for the plan?

**2**

Did you work enough hours to earn service credit this month?

# Service Credit Qualification, cont.

What number of hours makes sense for us?



Hmmm...do our employees tend to work a "normal schedule?"



Should we exclude part-time employees from the plan?



# Leaves of Absence - Today

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- A Leave of Absence is when an employee is **out for an extended period of time** for reasons such as disability, workers' compensation, and the Family Medical Leave Act (FMLA)
- Each type of leave has nuanced differences as it relates to granting service credit, reporting wages, and remitting employee and employer contributions
- We see inconsistent application of service credit and reporting of third party wages and contributions

# Leaves of Absence – 1/1/2021

- Leave of absence will become a plan provision that employers can **specify which type(s) of leave will be included or excluded** when determining both employer and employee contributions, and using the wages as part of an employee’s FAC calculation
- This will help align how the various types of leave are administered for your plan

| Type of Leave  | Included                 | Excluded                 |
|--|--------------------------|--------------------------|
| Short- and Long-Term Disability  | <input type="checkbox"/> | <input type="checkbox"/> |
| Workers' Compensation  | <input type="checkbox"/> | <input type="checkbox"/> |
| Unpaid Family Medical Leave Act (FMLA)   | <input type="checkbox"/> | <input type="checkbox"/> |
| Other: <input type="text"/><br>For example, sick and accident, administrative, educational, sabbatical, etc. | <input type="checkbox"/> | <input type="checkbox"/> |
| Other 2: <input type="text"/><br>Additional leave types as above   | <input type="checkbox"/> | <input type="checkbox"/> |

# Leaves of Absence – 1/1/2021, cont.

- When determining the employee's final average compensation (FAC) amount for benefit calculation, MERS will **skip those months of leave and lump sum payments** issued during a leave month and will not be used in the calculation of benefit
- Third-party wages are **no longer reported** for leaves of absence
- For contributory divisions, employee contributions **are required** in order to grant service credit

*Formula example:*

**Step 1:** 120 hrs. x \$25 = \$3,000 (*approx. wage*)

**Step 2:** \$3,000 x 5% (*employee % rate*) = \$150 (*employee contributions due for one month of leave*)

# Military Leave – No Changes

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- Military leave is governed by the Uniformed Services Employment and Reemployment Act (USERRA) and **affords an employee the right to service credit for qualified military leaves of absence** if the employee returns to their same employer within the timeframe allowed
- There will be **no changes** to the way in which Military Leave is administered

# Definition of Compensation – Today

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- Definition of Compensation is used to **calculate an employee's final average compensation** (FAC) and determine both **employer and employee contributions**
- Wages calculated using the elected definition and paid to employees **must be reported** to MERS
- For DB if an employer has not adopted a specific definition, it is assumed that their definition is the Full Definition

# Definition of Compensation – 1/1/2021

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- There will be three standard definitions of compensation – and an allowable fourth, custom option.
- This change:
  - **Provides clarity** to what should be included or excluded when reporting wages and contributions
  - Allows for **consistency and alignment**
  - **Maintains customization** for employers who need it



# Definition of Compensation – 1/1/2021, cont.

| <b>Standard Definitions</b><br><i>Standard definitions are non-modifiable</i>  | <b>Base Wages</b>          | <b>Box 1 Wages<br/>(from W-2)</b> | <b>Gross Wages</b>             | <b>Custom<br/>Definition</b> |
|--|----------------------------|-----------------------------------|--------------------------------|------------------------------|
| <b>Types of Compensation</b>   |                            |                                   |                                |                              |
| <b>Regular Wages</b><br>Salary or hourly wage X hours<br>PTO used (sick, vacation, personal, bereavement, holiday leave, or unclassified)<br>On-call pay   | All Regular Wages included | All Regular Wages included        | All Regular Wages included     | TBD                          |
| <b>Other Wages</b><br>Shift differentials<br>Overtime<br>Severance issued over time (weekly/bi-weekly)   | Excluded                   | All Other Wages included          | All Other Wages included       | TBD                          |
| <b>Lump Sum Payments</b><br>PTO cash-out<br>Longevity<br>Bonuses<br>Merit pay<br>Job certifications<br>Educational degrees<br>Moving expenses<br>Sick payouts<br>Severance (if issued as lump sum)                                 | Excluded                   | All Lump Sum Payments included    | All Lump Sum Payments included | TBD                          |
| <b>Taxable Payments</b><br>Travel through a non-accountable plan (i.e. mileage not tracked for reimbursement)<br>Prizes, gift cards<br>Personal use of a company car<br>Car allowance  | Excluded                   | All Taxable Payments included     | All Taxable Payments included  | TBD                          |
| <b>Reimbursement of Nontaxable Expenses</b> (as defined by the IRS)<br>Gun, tools, equipment, uniform<br>Phone<br>Fitness<br>Mileage reimbursement<br>Travel through an accountable plan (i.e. tracking mileage for reimbursement) | Excluded                   | Excluded                          | Excluded                       | TBD                          |

# Employee Contribution Requirements

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- For contributory plans, it is **important for accuracy and timeliness** that MERS has the most up-to-date employee contribution rate on record
- **If you are required to provide a *contribution discrepancy code* each month when submitting wage and contribution reports, MERS does NOT have the same information on file**



# Summary

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- Create a specific provision for **Plan Eligibility** and redefine options of inclusion or exclusion of certain position types
- Rename Day of Work provision to **Service Credit Qualification** and set the standard to the number of hours worked in a month
- Create **Leave of Absence** provisions with the ability for employers to elect whether service credit is granted
- Create multiple **Definitions of Compensation**



# FAQs

# FAQ #1

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**Is there a default if I don't send back the addendum?**

## FAQ #2

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**What if I don't want to complete the form electronically? Can I send in paper?**

## FAQ #3

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**Can I get a walk-through of the addendum and how to complete it?**

## FAQ #4

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**Can I get a copy of my adoption documents so I know what is currently in effect?**



# FAQ #5

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**Can I decide who will sign the addendum??**

# FAQ #6

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**Where will I see these provisions in the future?**

# Employer Reporting Resources



## Reporting Resource Page on [www.mersofmich.com](http://www.mersofmich.com)

- More FAQs
- Publications
- Contact information



## Regional Team

- Your regional team is ready to assist you with all of your plan needs and questions

Effective January 1, 2021, MERS is implementing several modifications to the way in which defined benefit plans are administered. Below you will find an overview of each of the modifications.

After reviewing the information below, you will be required to submit an updated Adoption Agreement Addendum to MERS indicating changes and/or provision clarifications you're making based on these modifications. Please note that any changes you make will be effective January 1, 2021, and future benefit changes do not impact prior benefits. Your addendum confirming your plan provisions is due to MERS by **September 30, 2020**.

**Resource**

- FAQs (pdf)
- Defined Benefit Employer Reporting Guide (pdf)

**Questions?**

Search out to your [benefit plan coordinator](#) with any questions.

**Webinars**

Learn more information and ask questions on reporting updates and provisional changes during these upcoming webinars:

**Defined Benefit Plan Provisions**  
Monday, September 21  
9:00 – 10:00 a.m.  
[Register](#)

- + Plan Eligibility Clarification
- + Day of Work Definition Modification
- + Leaves of Absence Clarification
- + Definition of Compensation
- + Have a Defined Contribution (DC) Plan?
- + Employee Contribution Requirements

# Contacting MERS of Michigan

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## MUNICIPAL EMPLOYEES' RETIREMENT SYSTEM

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[www.mersofmich.com](http://www.mersofmich.com)



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