MPSERS Pension Explainer: Why Michigan Needs to Finish Reforming School Employee Retirement Benefits

Reason

1. Pension Debt and Cost Keeps Growing

❖ MPSERS' unfunded liabilities—or pension debt—have increased from less than $2 billion to more than $29 billion over the past 15 years.[1] This pension debt is only going to continue increasing in coming years unless there is a meaningful change to the policies governing MPSERS.

❖ The primary reason MPSERS pension debt has grown is that assumptions used by the Office of Retirement Services have been overly optimistic about investment performance.

2. The Hybrid Plan Did Not Fully Fix the Problem

❖ Unfunded liabilities have more than tripled since the "hybrid" Pension Plus Plan was adopted, growing from $7.9 billion as of the end of 2011, to over $29 billion today.[2]

❖ The hybrid plan is exposing taxpayers to underperforming investment returns. The hybrid plan assumes a 7% long-term average rate of return on investments. This is more reasonable than the 8% assumed return that has been used for the rest of MPSERS, but it is still a risky bet compared to market forecasts. At best, the **7% return** assumption used by the Pension Plus hybrid plan has **a 50/50 chance** of being accurate.

- Average investment return:[3] **10-year average: 5.8%** | **15-year average: 6.5%**
- Many **market forecasts** suggest average returns for pension plans like MPSERS are likely to be around **6% (or less)** in the coming decades.

3. Doing Nothing Will Mean Growing Pension Costs for Schools

❖ If Michigan continues to ignore the problems with MPSERS, then pension costs are likely to more than double over the next two decades. Specifically, the actuarially determined contribution for the state and school districts will likely spike from around 30% of teacher payroll to around 60% of teacher payroll.[4] (See figure on other side)

❖ The growing costs to fund pension benefits are only going to continue crowding out the school aid fund, education resources, and the ability to increase teacher compensation.

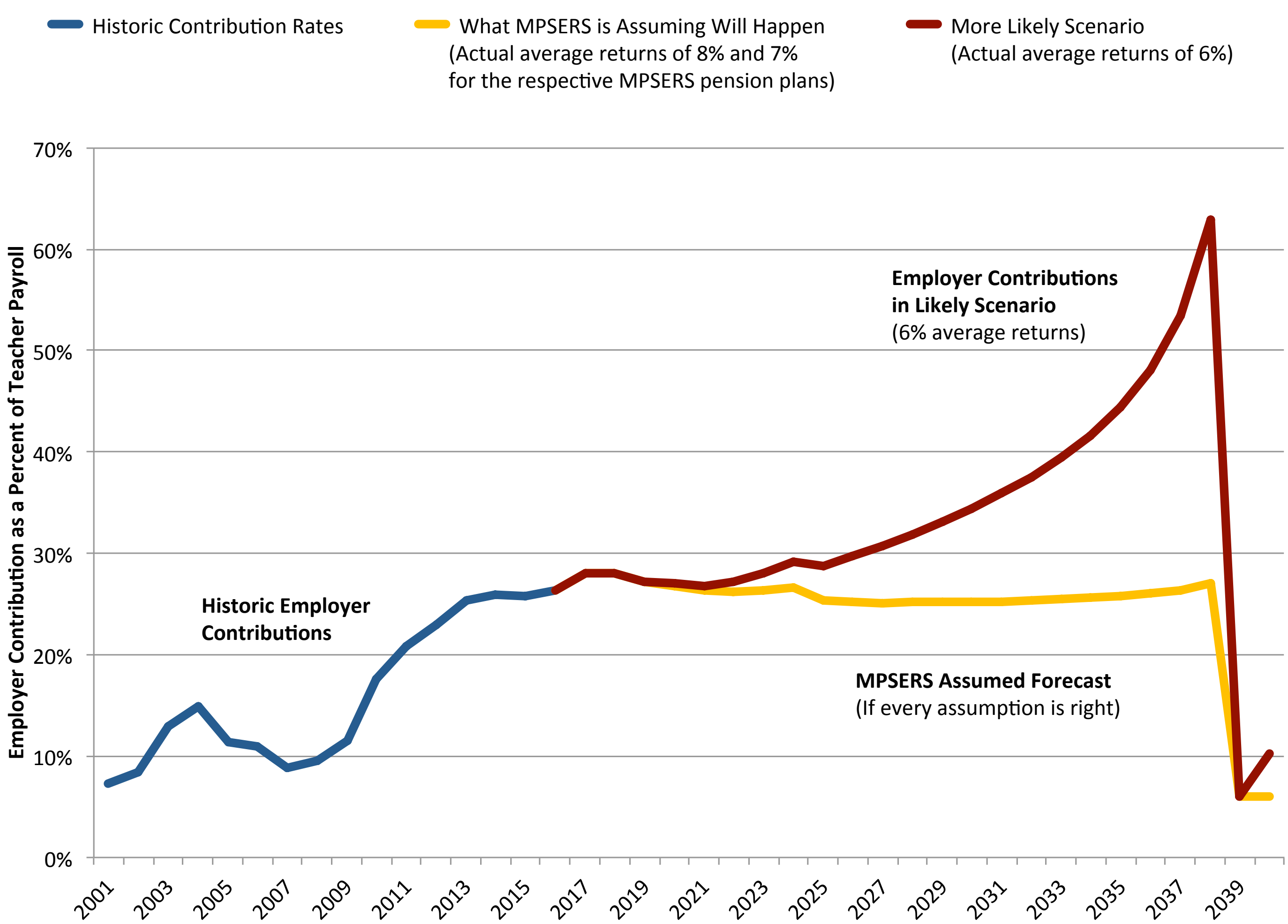
4. Pensions Are Hurting the State's Bond Rating

❖ Surging pension liabilities for the state budget are an "uncertainty" that is keeping Michigan's bond rating from improving, according to Moody's Investor Service.[5]

Questions about pension reform? Want to see the sources for the numbers quoted here?
Check out www.reason.org/MPSERS

[1] MPSERS Comprehensive Annual Financial Report for Fiscal Year End 2016
[2] MPSERS Comprehensive Annual Financial Report for Fiscal Year End 2016
[3] Geometric mean of market valued rates of return, see MPSERS Comprehensive Annual Financial Reports for Fiscal Year End 2002 to 2016
[4] Reason Foundation forecast of MPSERS baseline employer contribution rates based on plan assumptions and publicly available actuarial reports, with an annual average 6% actual return on assets through 2040
[5] Small Business Association of Michigan News, January 24, 2017: https://www.sbam.org/Resources/tabid/97/ArtMID/2980/ArticleID/2705/Economic-diversity-pension-liability-keeps-MI-from-higher-bond-rating.aspx

MPSERS Employer Contribution Rate Forecast:
School District Costs as a % of Payroll Depending on Actual Investment Returns



Source: Reason Foundation forecast of MPSERS baseline based on plan assumptions, compared to forecast of MPSERS baseline with 6% ROA

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