

**SUBSTITUTE FOR  
HOUSE BILL NO. 5266**

A bill to amend 1943 PA 240, entitled "State employees' retirement act," by amending sections 1a, 1e, 1i, 49, 53, 55, and 64 (MCL 38.1a, 38.1e, 38.1i, 38.49, 38.53, 38.55, and 38.64), section 1a as amended by 1998 PA 205, sections 1e and 1i as amended and sections 53, 55, and 64 as added by 1996 PA 487, and section 49 as amended by 2002 PA 93.

**THE PEOPLE OF THE STATE OF MICHIGAN ENACT:**

1       Sec. 1a. (1) "Accumulated contributions" means the sum of  
2 all amounts deducted from the compensation of a member and  
3 credited to the member's individual account in the employees'  
4 savings fund, together with regular interest on that account.  
5       (2) "Actuarial cost" means an amount that shall be paid,  
6 except as otherwise specifically provided by this act, by a  
7 member to purchase additional service credit as allowed under

1 this act. Actuarial cost shall be computed as provided in  
2 section 17j.

3 (3) "Annuity" means annual payments for life derived from the  
4 accumulated contributions of a member. An annuity shall be paid  
5 in equal monthly installments.

6 (4) "Annuity reserve" means the present value, computed upon  
7 the basis of mortality and other tables adopted by the retirement  
8 board, of all payments to be made on account of an annuity, or  
9 benefits in lieu of an annuity, granted to a member under this  
10 act.

11 (5) "Appointing authority" means the departmental officer who  
12 has the responsibility of making appointments and handling all  
13 other personnel transactions affecting the employees in the  
14 agency that the officer represents.

15 (6) **"Banked leave time program" means the part B annual leave**  
16 **hours within the annual and sick leave program for state**  
17 **employees approved by a ruling of the internal revenue service on**  
18 **September 5, 2003, in which a pay reduction or other concessions**  
19 **are applied to a member or qualified participant in exchange for**  
20 **additional part B annual leave hours.**

21 Sec. 1e. (1) "Final average compensation" means the average  
22 of those years of highest annual compensation paid to a member  
23 during a period of 5 consecutive years of credited service; or if  
24 the member has less than 5 years of credited service, then the  
25 average of the annual compensation paid to the member during the  
26 member's total years of credited service. For a person whose  
27 retirement allowance effective date is on or after October 1,

1 1987, "final average compensation" means the average of those  
2 years of highest annual compensation paid to a member during a  
3 period of 3 consecutive years of credited service; or if the  
4 member has less than 3 years of credited service, then the  
5 average of the annual compensation paid to the member during the  
6 member's total years of credited service. A member's final  
7 average compensation shall not be diminished because of required  
8 1-day layoffs. The compensation used in computing the final  
9 average compensation for a period during which a member is in a  
10 voluntary or involuntary pay reduction plan A or on a designated  
11 temporary layoff shall include the value of the hours not worked  
12 calculated at the member's hourly rate or rates of pay in effect  
13 immediately before the applicable final average compensation  
14 period. A member's final average compensation shall not be  
15 increased or decreased by the member's participation in voluntary  
16 or involuntary pay reduction plan B. Payment for accrued annual  
17 leave at separation in excess of 240 hours **and payment for part B**  
18 **annual leave hours at separation** shall not be included in final  
19 average compensation. **Beginning October 1, 2003, the**  
20 **compensation used to compute the final average compensation for a**  
21 **period during which a member is participating in the banked leave**  
22 **time program shall include the value of any unpaid furlough hours**  
23 **and the value of any unpaid hours exchanged for part B annual**  
24 **leave hours calculated at the member's then current hourly rate**  
25 **or rates of pay.**

26 (2) "Final compensation" means a member's annual rate of  
27 compensation at the time the member last terminates employment

1 with this state.

2       **(3) "Furlough hours" means unworked hours incurred in**  
3 **conjunction with the banked leave time program.**

4       **(4) —(3)—** "Internal revenue code" means the United States  
5 internal revenue code of 1986.

6       Sec. 1i. (1) "Service" means service rendered to this state  
7 by an elected or appointed state official or employee of this  
8 state. Credit for service shall be determined by appropriate  
9 rules and regulations of the retirement board, but not more than  
10 1 year of service shall be creditable for all service in 1  
11 calendar year. The retirement board shall not allow credit for  
12 service for any period of more than 1 month in any 1 calendar  
13 year during which the employee was absent without pay. However,  
14 full service credit shall be given for a period during which an  
15 employee is on leave of absence and is receiving worker's  
16 compensation benefits as the result of a duty-incurred  
17 disability. Full service credit shall also be given to an  
18 employee for required 1-day layoffs, for voluntary or involuntary  
19 participation in pay reduction plan A, pay reduction plan B, or  
20 both, in effect during the fiscal years ending on and after  
21 September 30, 1981, ~~and~~ for required and designated temporary  
22 layoffs, **and, beginning October 1, 2003, for furlough hours, and**  
23 **for participation in the banked leave time program.**

24       (2) "State treasurer" means the treasurer of this state.

25       (3) "Tier 1" means the retirement plan available to a member  
26 under this act who was first employed and entered upon the  
27 payroll before March 31, 1997 and who does not elect to become a

1 qualified participant of Tier 2.

2 (4) "Tier 2" means the retirement plan established pursuant  
3 to section 401(k) of the internal revenue code that is available  
4 to qualified participants under sections 50 to 69.

5 Sec. 49. (1) This section is enacted pursuant to  
6 section 401(a) of the internal revenue code, **26 USC 401**, that  
7 imposes certain administrative requirements and benefit  
8 limitations for qualified governmental plans. This state intends  
9 that the retirement system be a qualified pension plan created in  
10 trust under section 401 of the internal revenue code, **26 USC 401**,  
11 and that the trust be an exempt organization under section 501 of  
12 the internal revenue code, **26 USC 501**. The department shall  
13 administer the retirement system to fulfill this intent.

14 ~~(2) Except as otherwise provided in this section,~~  
15 ~~employer-financed benefits provided by the retirement system~~  
16 ~~under this act shall not exceed the lesser of \$90,000.00 or 100%~~  
17 ~~of the member's average compensation for high 3 years as~~  
18 ~~described in section 415(b)(3) of the internal revenue code for~~  
19 ~~retirement occurring at age 62 or older.~~

20 ~~—— (3) The limitation on employer-financed benefits provided by~~  
21 ~~the retirement system under subsection (2) applies unless~~  
22 ~~application of subsections (4) and (5) produces a higher~~  
23 ~~limitation, in which case the higher limitation applies.~~

24 ~~—— (4) If a member retires before age 62, the amount of~~  
25 ~~\$90,000.00 in subsection (2) is actuarially reduced to reflect~~  
26 ~~payment before age 62. The retirement system shall use an~~  
27 ~~interest rate of 5% per year compounded annually to calculate the~~

~~1 actuarial reduction in this subsection. If this subsection  
2 produces a limitation of less than \$75,000.00 at age 55, the  
3 limitation at age 55 is \$75,000.00 and the limitations for ages  
4 under age 55 shall be calculated from a limitation of \$75,000.00  
5 at age 55.~~

~~6 (5) Section 415(d) of the internal revenue code requires the  
7 commissioner of internal revenue to adjust the \$90,000.00  
8 limitation in subsection (2) to reflect cost of living increases,  
9 beginning with calendar year 1988. This subsection shall be  
10 administered using the limitations applicable to each calendar  
11 year as adjusted by the commissioner of internal revenue under  
12 section 415(d) of the internal revenue code. The retirement  
13 system shall adjust the benefits subject to the limitation each  
14 year to conform with the adjusted limitation.~~

15 (2) The retirement system shall be administered in compliance  
16 with the provisions of section 415 of the internal revenue code,  
17 26 USC 415, and regulations under that section that are  
18 applicable to governmental plans. Employer-financed benefits  
19 provided by the retirement system under this act shall not exceed  
20 the applicable limitations set forth in section 415 of the  
21 internal revenue code, 26 USC 415, as adjusted by the  
22 commissioner of internal revenue under section 415(d) of the  
23 internal revenue code, 26 USC 415, to reflect cost-of-living  
24 increases, and the retirement system shall adjust the benefits  
25 subject to the limitation each calendar year to conform with the  
26 adjusted limitation. For purposes of section 415(b) of the  
27 internal revenue code, 26 USC 415, the applicable limitation

1 shall apply to aggregated benefits received from all qualified  
2 pension plans for which the office of retirement services  
3 coordinates administration of that limitation. If there is a  
4 conflict between this section and another section of this act,  
5 this section prevails.

6       (3) ~~-(6)-~~ The assets of the retirement system shall be held  
7 in trust and invested for the sole purpose of meeting the  
8 legitimate obligations of the retirement system and shall not be  
9 used for any other purpose. The assets shall not be used for or  
10 diverted to a purpose other than for the exclusive benefit of the  
11 members, vested former members, retirants, and retirement  
12 allowance beneficiaries before satisfaction of all retirement  
13 system liabilities.

14       (4) ~~-(7)-~~ The retirement system shall return post-tax member  
15 contributions made by a member and received by the retirement  
16 system to a member upon retirement, pursuant to internal revenue  
17 service regulations and approved internal revenue service  
18 exclusion ratio tables.

19       (5) ~~-(8)-~~ The required beginning date for retirement  
20 allowances and other distributions shall not be later than April  
21 1 of the calendar year following the calendar year in which the  
22 employee attains age 70-1/2 or April 1 of the calendar year  
23 following the calendar year in which the employee retires.

24       (6) ~~-(9)-~~ If the retirement system is terminated, the  
25 interest of the members, vested former members, retirants, and  
26 retirement allowance beneficiaries in the retirement system is  
27 nonforfeitable to the extent funded as described in section

1 411(d)(3) of the internal revenue code, **26 USC 411**, and related  
2 internal revenue service regulations applicable to governmental  
3 plans.

4 (7) ~~-(10)-~~ Notwithstanding any other provision of this act to  
5 the contrary that would limit a distributee's election under this  
6 act, a distributee may elect, at the time and in the manner  
7 prescribed by the retirement board, to have any portion of an  
8 eligible rollover distribution paid directly to an eligible  
9 retirement plan specified by the distributee in a direct  
10 rollover. This subsection applies to distributions made on or  
11 after January 1, 1993.

12 (8) ~~-(11)-~~ For purposes of determining actuarial equivalent  
13 retirement allowances under sections 31(1)(a) and (b) and 20(2),  
14 the actuarially assumed interest rate shall be 8% with  
15 utilization of the 1983 group annuity and mortality table.

16 ~~-(12)- Notwithstanding any other provision of this section,~~  
17 ~~the retirement system shall be administered in compliance with~~  
18 ~~the provisions of section 415 of the internal revenue code and~~  
19 ~~revenue service regulations under that section that are~~  
20 ~~applicable to governmental plans. If there is a conflict between~~  
21 ~~this section and another section of this or any other act of this~~  
22 ~~state, this section prevails.~~

23 (9) ~~-(13)-~~ Notwithstanding any other provision of this act,  
24 the compensation of a member of the retirement system shall be  
25 taken into account for any year under the retirement system only  
26 to the extent that it does not exceed the compensation limit  
27 established in section 401(a)(17) of the internal revenue code,

1 **26 USC 401**, as adjusted by the commissioner of internal revenue.  
2 This subsection applies to any person who first becomes a member  
3 of the retirement system on or after October 1, 1996.

4 **(10) —(14)—** Notwithstanding any other provision of this act,  
5 contributions, benefits, and service credit with respect to  
6 qualified military service will be provided under the retirement  
7 system in accordance with section 414(u) of the internal revenue  
8 code, **26 USC 414**. This subsection applies to all qualified  
9 military service on or after December 12, 1994.

10 Sec. 53. (1) For the purposes of this section and sections  
11 54 to 69, the words and phrases defined in this section and  
12 sections 54 to 69 have the meanings ascribed to them in those  
13 sections.

14 (2) "Accumulated balance" means the total balance in a  
15 qualified participant's, former qualified participant's, or  
16 refund beneficiary's individual account in Tier 2.

17 (3) "Compensation" means the remuneration paid a participant  
18 on account of the participant's services rendered to his or her  
19 employer — ~~Compensation includes only wages, tips, and other~~  
20 ~~compensation as reported by the employer on the participant's~~  
21 ~~federal form W-2, wage and tax statement.~~ **equal to the sum of**  
22 **the following:**

23 (a) A participant's W-2 earnings for services performed for  
24 the employer excluding part B annual leave hours paid at  
25 separation.

26 (b) Any amount contributed or deferred at the election of the  
27 participant which is excluded from gross income under section

1 125, 132(f)(4), 401(k), 403(b), or 457 of the internal revenue  
2 code, 26 USC 125, 132, 401, 403, and 457.

3 (c) Beginning October 1, 2003, the value of any unpaid  
4 furlough hours and the value of any unpaid hours exchanged for  
5 part B annual leave hours calculated at the participant's then  
6 current hourly rate or rates of pay for a period during which a  
7 participant is participating in the banked leave time program.

8 (d) The value of hours not worked during which a participant  
9 is in a voluntary or involuntary pay reduction plan A or on 1-day  
10 layoff or designated temporary layoff calculated at the  
11 participant's then current hourly rate or rates of pay.

12 Sec. 55. (1) "Plan document" means the document that  
13 contains the provisions and procedures of Tier 2 in conformity  
14 with this act and the internal revenue code.

15 (2) ~~-(1)-~~ "Qualified participant" means an individual who is  
16 a participant of Tier 2 and who meets 1 of the following  
17 requirements:

18 (a) An individual who is first employed and entered upon the  
19 payroll of his or her employer on or after March 31, 1997, and  
20 who before March 31, 1997 would have been eligible to be a member  
21 of Tier 1.

22 (b) An individual who elects to terminate membership in Tier  
23 1 and who elects to participate in Tier 2 in the manner  
24 prescribed in section 50.

25 (3) ~~-(2)-~~ "Refund beneficiary" means an individual nominated  
26 by a qualified participant or a former qualified participant  
27 under section 66 to receive a distribution of the participant's

1 accumulated balance in the manner prescribed in section 67.

2 (4) ~~(3)~~ "State treasurer" means the treasurer of this  
3 state.

4 (5) Except as otherwise provided in this subsection, "year of  
5 service" means each period during which a qualified participant  
6 is employed by the employer and is credited with 2,080 hours of  
7 service. The Tier 2 plan administrator and the plan document may  
8 provide for a lesser number of annual hours and a maximum number  
9 of hours per pay period for any classification of employees,  
10 provided that no participant shall receive credit for more than 1  
11 year of service for any 12-month period of employment. Beginning  
12 January 1, 2003, full service credit shall also be given to a  
13 participant for furlough hours, for required 1-day layoffs, for  
14 required and designated temporary layoffs, for a year in which a  
15 participant temporarily leaves employment to enter active  
16 military duty and then dies during that active military duty, and  
17 for participation in the banked leave time program. In the event  
18 a terminated participant is reemployed, such individual shall  
19 retain credit for all full and partial years of service completed  
20 prior to such reemployment, for purposes of determining his or  
21 her vesting percentage in any employer contributions made  
22 pursuant to section 63(2) and (3) after his or her reemployment.

23 Sec. 64. (1) A qualified participant is immediately 100%  
24 vested in his or her contributions made to Tier 2 and employer  
25 contributions under the banked leave time program. ~~A~~ Except as  
26 otherwise provided in this section, a qualified participant shall  
27 vest in the employer contributions made on his or her behalf to

1 Tier 2 according to the following schedule:

2 (a) Upon completion of 2 years of service, 50%.

3 (b) Upon completion of 3 years of service, 75%.

4 (c) Upon completion of 4 years of service, 100%.

5 (2) A qualified participant is vested in the health insurance  
6 coverage provided in section 68 if the qualified participant  
7 meets 1 of the following requirements:

8 (a) The qualified participant has completed 10 years of  
9 service as a qualified participant and was not a member, deferred  
10 member, or former nonvested member of Tier 1.

11 (b) The qualified participant was a member, deferred member,  
12 or former nonvested member of Tier 1 who made an election to  
13 participate in Tier 2 pursuant to section 50, and who has met the  
14 service requirements he or she would have been required to meet  
15 in order to vest in health benefits under section 20d.