

PROTECTING LOCAL GOVERNMENT RETIREMENT AND BENEFITS ACT AND COMPANION BILLS

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**House Bills 5298 (H-1) and 5311 as
reported from committee
Sponsor: Rep. Thomas A. Albert**

**House Bills 5303, 5304, & 5305 as
reported from committee
Sponsor: Rep. Kathy Crawford**

**House Bills 5299 (H-1), 5300, & 5310 as
reported from committee
Sponsor: Rep. James A. Lower**

**House Bills 5306 & 5307 as reported from
committee
Sponsor: Rep. Gary Howell**

**House Bills 5301 & 5302 as reported from
committee
Sponsor: Rep. Gary Glenn**

**House Bills 5312 & 5313 as reported from
committee
Sponsor: Rep. Rob VerHeulen**

**Committee: Michigan Competitiveness
Complete to 12-6-17**

BRIEF SUMMARY:

House Bill 5298 would create the Protecting Local Government Retirement and Benefits Act (the proposed Act) in Michigan law.

Approximately one-third of the 1,856 general purpose governments in Michigan provide employees with post-retirement benefits—whether in the form of pension benefits or other post-employment benefits (OPEB), which principally include health care benefits. According to a July 2017 report from the governor’s Responsible Retirement Reform for Local Government Task Force, the total unfunded pension liability for local units in Michigan is estimated at \$7.5 billion, and the total unfunded liability for retiree health care at \$10.1 billion.¹

House Bill 5298 states that, while those benefits are an optional activity or service of local units, the unfunded obligations of a local unit related to those benefits can adversely affect the residents as well as the financial solvency of the local unit. Accordingly, the bill states that the legislature finds it necessary to authorize assistance, in the form of the bill package, to serve the interest of the state and protect the credit of its local units.

¹ The report can be found at http://www.michigan.gov/documents/snyder/R3_Task_Force_Report_579101_7.pdf, and is discussed in greater detail in the ***Background*** of this summary. According to the report, these numbers do not account for the city of Detroit. The city had estimates ranging from \$5.7 to \$6.4 billion in unfunded OPEB liabilities with no prefunding at the time of its municipal bankruptcy; these were largely eliminated in the bankruptcy.

House Bill 5298 would do all of the following:

- Require that, if a local unit offers retirement health benefits, the normal cost of those benefits must be funded at certain levels by certain dates.
- Allow local units to apply for and receive a temporary waiver if the state treasurer finds that meeting funding benchmarks would cause the local unit an undue hardship.
- Prohibit local units from reopening or reoffering a closed defined benefit retiree pension or health system or plan beginning June 30, 2018.
- Prohibit local units from providing a component of health benefits to former employees or their dependents if that individual is enrolled in a program with the same component under another employer-sponsored program (or if the individual is eligible for, but is not enrolled in, another employer-sponsor program that would offer comparable benefits for that component).
- Prohibit local units from providing a defined benefit pension benefit to an individual first elected or appointed to a local unit's elective office (excluding county sheriff) after June 30, 2018 if the individual is new to the plan or system.
- Require the state treasurer to determine the underfunded status of each local unit's retirement health system and retirement pension system, based on whether the system meets certain benchmarks for actuarial accrued liability.
- Create the ***Local Government Retirement Stability Board*** (the Board) within the Michigan Department of Treasury (although functioning independently of Treasury), which would monitor compliance of an underfunded local unit and of any ***corrective action plan*** proposed by the local unit and approved by the Board.
- Require the state treasurer to declare a financial emergency triggering action under House Bill 5299 if a local unit cannot reach agreement on a corrective action plan, the Board does not approve a corrective action plan, or the Board determines that a corrective action plan is not being implemented in a way that will accomplish its objectives.
- Provide that part or all of a contract or agreement entered into, modified, extended, or renewed after the bill takes effect that conflicts with the bill would be void. Additionally, the bill would take precedence over a contrary provision of a local unit.

House Bill 5299 would require that a ***financial management team*** be created for an underfunded local unit for which the state treasurer declares that a financial emergency exists (and, if the team finds that a financial emergency exists, the governor would appoint an ***emergency manager*** for the municipality).

House Bill 5310 would allow a municipality to discontinue participation in the Municipal Employees Retirement System (MERS), for either all or a subset of its participating members.

House Bill 5311 would accelerate the sunset of a provision allowing municipalities to issue municipal securities to cover the costs of their unfunded pension liability and unfunded accrued health care liability

House Bills 5300-5309 and 5312 would mainly make other local government retirement statutes subject to the proposed Act.

THE APPARENT PROBLEM:

Large unfunded liabilities are primarily due to local governments not prefunding retiree health benefits (setting aside funding for benefits as they are accrued) and instead waiting to pay for benefits as the annual health care costs are incurred. Even those local governments that do prefund retiree health care benefits often have substantial unfunded liabilities mainly due to the following: 1) they do not make the full annual required payments, 2) system assets do not generate the investment returns assumed, and 3) the cost of health care increases at a rate significantly higher than general inflation. According to the July 2017 Responsible Retirement Reform for Local Government Task Force, in 2015, retiree health care actuarial accrued liabilities for Michigan cities, villages, and townships were on average 19% funded, and those of Michigan counties were on average 34% funded.²

THE CONTENT OF THE BILL:

House Bill 5298

Funding of other post-employment benefits (OPEB) required

The bill would require the following schedule for the funding of the normal cost of local units' retiree health care obligations, where **normal cost** means the annual service cost of retirement health benefits as they are earned during active employment of employees of the local unit of government in the applicable fiscal year, using an individual entry-age normal and level percent of pay actuarial cost method:

Fiscal year beginning:	Percent of Normal Cost
Between June 30, 2019 and July 1, 2020	20%
Between June 30, 2020 and July 1, 2021	40%
Between June 30, 2021 and July 1, 2022	60%
Between June 30, 2022 and July 1, 2023	80%
After June 30, 2023	100%

Permitted health retirement benefits

The bill would provide that, beginning July 1, 2018, if the local unit has opted to offer or provide retirement health benefits to former or current employees, the local unit may not do either of the following:

- Reopen a defined benefit retirement system or reoffer any other defined benefit plan to provide new retirement health benefits after that system or plan has been closed to new hires.
- Provide a component of retirement health benefits to a former employee or retiree health dependent if that individual is enrolled in the same component of active or retiree group health or welfare benefits provided by another employer (or if the individual is

² The report can be found at http://www.michigan.gov/documents/snyder/R3_Task_Force_Report_579101_7.pdf.

eligible for, though not enrolled in, a benefit at least comparable to the component available from the local unit).

Under the bill, a local unit would be permitted to change a current or future retirement health benefit provided under any applicable plan. However, the local unit would not be allowed to alter the right to certain vested retirement health benefits included in a collective bargaining agreement entered into before the bill takes effect, for the duration of that agreement.

Temporary waiver from funding requirements

The bill would allow a local unit to submit a temporary waiver application to the state treasurer showing that the normal cost funding requirements in the chart above would cause an *undue hardship* to the local unit by diverting significant resources from the provision of existing essential services. The state treasurer would review the application and make a recommendation to the Board, which would vote to approve or deny the waiver. The Board may only grant 1 waiver to a local unit under this provision, for not more than 5 years.

Supplemental actuarial analysis

The bill would require local units to provide a supplemental actuarial analysis before adopting any material proposed benefit change. The analysis must be provided by the system's actuary and include an analysis of the long-term costs of the material proposed benefit change. The local unit must provide the analysis to the decision-making body that would approve the benefit change at least 7 days before the change is adopted. Finally, if the change is adopted, the local unit would be required to pay at least the incremental cost increase in the annual required contribution associated with the change.

(Here, *material proposed benefit change* would mean an increase in the amount of current or future retirement health benefits provided to persons entitled to them that would cause a reasonable person in the governing body's position to conclude that the increase would materially increase an unfunded liability of the local unit or its retirement system.)

Summary retiree health care report

The bill would require that local units submit a summary retiree health care report annually to the local unit's governing body and Treasury within 6 months after the end of its fiscal year. Treasury, in turn, would post an executive summary of each valuation report—which must include the applicable system's unfunded actuarial accrued liability for retiree health—on its website. Additionally, Treasury would submit each executive summary to the House and Senate Appropriations committees and House and Senate Fiscal Agencies at least 30 days after posting.

The report must contain all of the following for each retirement system that provides retirement health benefits:

- Name of the system and its fiduciaries and service providers.
- Assets and liabilities and changes in net plan assets on a plan-year basis.
- Funded ratio based on the ratio of valuation assets to actuarial accrued liabilities on a plan-year basis.

- Assumed rate of return and actual rate of return for the previous 1-, 5-, and 10-year periods.
- Discount rate used by the system.
- Amortization method for unfunded liability, indicating whether it is open or closed.
- Amortization method, indicating whether it is level percent or level dollar, and the assumed payroll growth rate.
- Remaining amortization time period.
- Annual required contribution for the retirement system, indicating the normal cost and unfunded actuarial accrued liability.

Irrevocable trusts for retirement systems

The bill would authorize and create an irrevocable trust for each retirement system. The trusts would be established and administered in accordance with the Internal Revenue Code's Section 115, which governs quasi-governmental organizations. All normal cost funding detailed in the chart above, as well as any other prefunding of retirement health benefits, must be deposited in the trust.

The governing board of each retirement system would be the grantor and would administer the trust in order to pay retirement health benefits. The system's board (or local unit's governing body if the system does not have a board) would also act as trustees and adopt a trust agreement.

Assets contributed to the trust would be irrevocable and used solely to provide retirement health benefits and pay for applicable administrative costs. Assets of the trust and the ability of a beneficiary to receive the benefits are not assignable or subject to garnishment or attachment. The assets and income of the trust are exempt from taxation, and distributions may not be treated as taxable income, by Michigan or one of its political subdivisions.

Under the bill, trustees would not be personally liable for losses suffered by the trust, unless the loss arises out of the trustee's willful misconduct or intentional wrongdoing. Likewise, trustees would not be responsible for the trust's adequacy to meet its obligations or required to take action to enforce the payment of contributions or appropriations to the trust.

Any assets remaining in the trust after all obligations and liabilities have been satisfied would be distributed to the state, local unit, or other Section 115 tax-exempt employers within the applicable retirement system.

New provisions for retirement pension benefits

The bill would introduce new requirements for local units that offer or provide employees or former employees with retirement pension benefits, beginning July 1, 2018. First, a local unit may not provide defined benefit retirement pension benefits to an individual first elected or appointed to a local unit's elective office (excluding county sheriff) after June 30, 2018 if the individual is new to the plan or system. Additionally, if a proposed benefit change is adopted, the local unit must pay the incremental cost increase in the annual

required contribution associated with the proposed benefit change. Also, a local unit may not reopen or reoffer a closed defined benefit system or plan.

Finally, for all fiscal years beginning after December 31, 2020, a local unit could not use or apply a rolling amortization method, open amortization period, or other adjustable amortization period for an unfunded actuarial accrued liability of retirement pension benefits under a retirement system. Nor would the bill allow a local unit to extend an amortization period after that date. However, the state treasurer could, at the local unit’s request, grant 1 extension of the 2020 deadline to a new deadline no later than December 31, 2025. The state treasurer could also extend an amortization period in effect when this bill takes effect if requested by the local unit, agreed to by the retirement system fiduciary, and determined to be in the best financial interest of the local unit.

Responsibilities of the state treasurer

The bill would require the state treasurer to promulgate rules under the Administrative Procedures Act of 1969 to establish *standards for local units for actuarial assumptions* and other methods of valuation of retirement systems, including standard ranges for investment returns, amortization of unfunded liabilities, mortality updates, discount rates, and health care inflation.

The state treasurer must create an evaluation system and provide for review and oversight of an underfunded local unit beginning on the date the state treasurer determines that the local unit is underfunded. The state treasurer must determine whether local units are underfunded beginning December 31, 2017 and annually thereafter.

The state treasurer would determine that a local unit is underfunded if any of the following apply:

- The actuarial accrued liability of a local unit’s retirement health system or retirement pension system is less than adequately funded, according to the most recent annual report and, if the local unit is a city, village, township, or county, the annual required contribution for either all of the local unit’s pension systems or all of the local unit’s retiree health systems is greater than 10% of the local unit’s annual general fund operating expenditures, based on the most recent fiscal year. *Adequately funded* would mean the following amounts for the following fiscal years:

Fiscal year beginning:	Retiree Health System Minimum Funding Ratio:	Pension system Minimum Funding Ratio:
Between June 30, 2016 and July 1, 2023	30% funded	60% funded
Between June 30, 2023 and July 1, 2028	35% funded	65% funded
Between June 30, 2028 and July 1, 2033	40% funded	70% funded
Between June 30, 2033 and July 1, 2038	45% funded	75% funded
Between June 30, 2038 and July 1, 2048	50% funded	
After June 30, 2038		80% funded
After June 30, 2048	80% funded	

- The local unit has not reported the annual cost of the liability of the retirement health system or retirement pension system using data required under the rules promulgated by the state treasurer.
- The state treasurer or the Board determines that the local unit does not have adequate financial resources to make its annual required contributions for retirement pension benefits or retirement health benefits, and the local unit's governing board requests to have underfunded status under the bill.

Finally, the state treasurer must post on the Treasury website the rules for establishing standards for local units for actuarial assumptions, the underfunded status and current waiver status of local units, any corrective action plan (described below), and all declarations of financial emergencies within local units.

(The local unit must also post on its website, or in a public place if it does not have a website, the information listed above, as applicable.)

Waiver of determination of underfunded status

The state treasurer must issue a waiver of the determination of underfunded status if the state treasurer determines that a local unit's underfunded status is being adequately addressed based on a review of relevant factors including the following:

- The degree to which the local unit provides retirement benefits.
- The local unit's proximity to the funded ratio and expenditure percentage as provided under the evaluation system.
- The local unit's demonstrated ability to address any underfunded status in prior fiscal years.
- The local unit's adherence to any prior corrective action plans after a determination of underfunded status.
- A review of the amount of any general fund operating expenditures of the local unit that are dedicated to the prefunding of retirement benefits.
- A review of the local unit's summary retiree health care report, including any trend lines as provided in that report.

Under the bill, the state treasurer must rescind the waiver upon a determination that the underfunded local unit has violated the Act or any mandatory financial controls in a way that substantially impairs its ability to pay certain obligations or that it has violated any provision of a corrective action plan, or that there is a substantial likelihood that either will imminently occur. The state treasurer must reverse the rescission and reinstate the waiver upon a determination that these circumstances no longer exist.

The state treasurer would have to provide the Board with a written report stating the reason for any waiver granted or reinstated.

Establishment of Local Government Retirement Stability Board

The bill would create the Board within Treasury. Generally, the Board would function independently of the state treasurer, but the budget, procurement, and related management

functions would be performed under the direction and supervision of the state treasurer. Additionally, Treasury would provide administrative support to the Board.

Three members of the Board would be appointed by the governor (including one from a list of nominees from the speaker of the House and one from a list from the Senate majority leader), with the governor's direct appointee serving as the chairperson. All three must be Michigan residents with knowledge, skill, or experience in accounting, actuarial science, retirement systems, retirement health benefits, or government finance. One would serve an initial term of 4 years, one of 3 years, and one of 2 years. Thereafter, terms would be 4 years.

The Board must meet at least quarterly. Members of the Board would serve without compensation but may receive reimbursement for travel and expenses incurred in the discharge of official duties. Members are subject to the Contracts of Public Servants with Public Entities Act and the Conflict of Interest Act.

Board responsibilities

The bill would require the Board to review the state treasurer's report on the reasons for granting or reinstating a waiver, and allow it to rescind either of those actions. Additionally, the Board must monitor compliance of an underfunded local unit with the requirements of the proposed Act and any corrective action plan, and certify substantial compliance by October 1 of each year. (The Board may require a local unit to provide verification of compliance with these requirements.) The board could contract for professional services, including, but not limited to, accounting, actuarial, appraisal, auditing, investment advisor, and legal services.

Corrective action plan

Under the bill, the Board must review and vote on a corrective action plan submitted by a local unit. The plan must be submitted within 180 days after determination of underfunded status, but the Board may extend the deadline by an additional 45 days if the local unit submits a reasonable draft of the plan and requests an extension. The plan must be negotiated with active employees and retirees and then approved by the local unit's governing body before it is submitted to the Board. Then, the Board must approve or reject the plan within 45 days after submission. At that point, subject to any corrective action plan and collective bargaining agreements in effect, the local unit has 180 days after approval to implement the plan or otherwise negotiate with employees and retirees to achieve the necessary cost reductions and funding improvements to permanently correct its underfunded status in all future years.

A corrective action plan would present options by which the local unit would address and permanently resolve its underfunded status. The options may include any of the following:

- Requiring additional employer or employee contributions.
- Adjusting the debt structure of the system.
- Altering eligibility, calculation of benefits, copays, or drug prescription coverage or other modification of provisions of the system.
- Submitting the question of issuing bonds or an additional millage to voters.

- Limiting the annual amount the local government may pay toward providing health benefits, including 1 or more of the following:
 - Implementing a maximum payment permitted for each coverage category of retirement health benefits, subject to health care inflation based on the US Consumer Price Index – medical care component.
 - Requiring the local unit to pay no more than 80% of the total annual cost for all retirement health benefits.
 - Implementing a cap on the total amount the local unit may pay.
- Requiring individuals included in a beneficiary unit to enroll in Medicare Part A and Part B in order to be eligible for benefits.
- Prohibiting the local unit from subsidizing health insurance benefits for employees hired after a specified future date.

Declaration of financial emergency

The bill would require the state treasurer to declare that a financial emergency exists in a local unit and create a financial management team (as described in HB 5299), if any of the following events occur:

- The local unit cannot reach agreement on a proposed corrective action plan.
- The Board does not approve the local unit’s plan.
- The Board determines that an approved plan is not being implemented in a manner that will accomplish its objectives.

Presumed validity of Board and corrective action plan

The validity of the Board and of a corrective action plan would be conclusively presumed unless questioned in an original action filed with the court of claims within 60 days after the bill or plan takes effect, respectively. The court of claims would have exclusive jurisdiction to hear these actions, as well as actions questioning the validity of the bill, and must do so in an expedited manner. Treasury would be a necessary party in such an action.

Appropriation

The bill would appropriate \$1.5 million from the general fund to Treasury in order to implement the bill. [Note: Inclusion of the appropriation means that the bill could not be subject to referendum.]

Constitutional protection of retirement benefits

Section 24 of Article IX of the Michigan Constitution of 1963 states that:

The accrued financial benefit of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby.

Financial benefits arising on account of service rendered in each fiscal year shall be funded during that year and such funding shall not be used for financing unaccrued liabilities.

The bill states that an obligation of a local unit that relates to retirement pension benefits or retirement benefits is not an obligation of the state, and the bill would not authorize the lending of the state's credit. It also provides that the bill would not authorize the diminishment or impairment of a contractual obligation under Section 24.

House Bill 5299

The bill would amend the Local Financial Stability and Choice Act, more commonly referred to as the *Emergency Manager Law*.³ That act provides that, upon confirmation of a financial emergency in a local unit, the local unit must select one of four options, including an emergency manager option (under Section 9 of the Act). HB 5299 would add a Section 9a to the Act to allow for the creation of a *financial management team* if: (1) a local unit is found to be experiencing a financial emergency specific to underfunding either pension or post-retirement health benefits, and (2) the local unit has not submitted or implemented a sufficient corrective action plan (as determined by the Local Government Retirement Stability Board under Section 11 of HB 5298).

Financial management team

The financial management team would include the following 3 members, appointed by the governor within 45 days after the state treasurer declares a financial emergency:

- A person with at least 5 years' experience and demonstrable expertise in financial matters.
- A person with at least 5 years' experience working in local units.
- A person who has been a resident of the municipality for at least 5 years and who is not an employee or elected or appointed officer of the local unit. (The local unit's governing body may submit a list of 3 nominees for this position to the governor).

A person would not be eligible to be appointed to a financial management team if the person had been convicted of a felony or misdemeanor for actions related to a previous emergency manager appointment.

Appointees under the first two categories may serve on more than one financial management team. All members must be paid for their service, with contracts approved by the state treasurer and posted on Treasury's website.

Members of the team must act in the best interest of the local unit, and are subject to the applicable provisions of the Lobby Act; Conflict of Interest Act; Contracts of Public Servants with Public Entities Act; and Standards of Conduct for Public Officers and Employees Act.

The team must meet initially at least 30 days after appointment and quarterly thereafter (or more frequently at the call of the chair or if requested by at least 2 members of the team). The team would exist until it determines and notifies the state treasurer that the local unit is no longer in underfunded status, and the state treasurer concurs.

³ House Fiscal Agency Analysis for the Emergency Manager Law, Public Act 436 of 2012 (SB 865):
<http://www.legislature.mi.gov/documents/2011-2012/billanalysis/House/pdf/2011-HLA-0865-F3E91E8A.pdf>

Powers of the financial management team

The bill would authorize a financial management team to take 1 or more of the following actions to resolve a local unit's underfunded status:

- Analyze factors and circumstances contributing to the underfunded status and require the local unit to take measures to correct the underfunded status, including the options described in the Corrective action plan section above.
- Require the local unit to amend, revise, approve, or disapprove its proposed budget or general appropriations act, which may include requiring the local unit to include or restrict specified amounts of money or payments for specified purposes or to transfer a fund balance of the unit.
- Require the local unit to employ or contract for auditors, actuaries, or other technical personnel to address the underfunded status.
- Require the local unit to sell, lease, assign, or otherwise use or transfer its assets or liabilities.
- Require the local unit to take any other action relating to its operation, its employment or personnel, or its expenditures necessary to address the underfunded status.

A financial management team may enter into a consent agreement with the local unit, which would provide for remedial measures necessary to address the underfunded status. The consent agreement may grant powers delegated to the team to an officer of the local unit.

Under the bill, any action taken by a financial management team would be binding on the local unit, and any budget, general appropriations act, or budget amendment recommended or adopted must be consistent with the requirements imposed by the team or required under a consent agreement.

Emergency Manager

If a financial management team determines that a local unit has failed to comply with this bill's mandates, or has not rectified its noncompliance with the bill's mandates after notification by the team, the team must declare that a financial emergency exists within the local unit and that the governor should appoint an emergency manager. If an emergency manager were appointed, the team would be dissolved.

Website

The bill would require Treasury to create and maintain a website that would allow residents of a municipality for which a financial management team is in place to submit input.

Appropriation

The bill would appropriate \$250,000 from the general fund to Treasury in order to implement the bill's provisions. [Note: Inclusion of the appropriation means that the bill could not be subject to referendum.]

House Bills 5300 to 5313

Generally, the other bills in the package would incorporate the new Protecting Local Government Retirement and Benefits Act (the proposed Act) throughout Michigan law.

House Bill 5300 would amend the *Incompatible Public Offices Act* to state that the prohibition on public officers or employees holding two or more incompatible offices at the same time would not apply to members of a financial management team or the Local Government Retirement Stability Board. (MCL 15.183)

House Bill 5301 would amend the *Reciprocal Retirement Act* to provide that a reciprocal unit and a reciprocal retirement system must comply with any applicable requirements of the proposed Act. (proposed MCL 38.1102a)

House Bill 5302 would amend the *Public Employee Retirement System Investments Act*. Currently, a system must provide a supplemental actuarial analysis before adoption of any proposed pension benefit change. The bill would amend this requirement so that the analysis is only required when an increase is proposed, instead of any change. Additionally, the bill would remove a requirement that a system post an information report on its website if its retiree health or pension is not at least 60% funded, as well as steps the system is taking to address the shortfall. This requirement was added by Public Act 530 of 2016 (House Bill 6075)⁴ and would be replaced by a schedule for required funding in the proposed Act. (MCL 38.1133 and 38.1140h)

House Bill 5303 would amend the *Revised Statutes of 1846* to make the provision of retirement benefits by a township under the statute subject to the proposed Act. (MCL 41.110b)

House Bill 5304 would provide that, if a county provides a system of retirement under the *Charter Counties Act*, that system is subject to the proposed Act. (MCL 45.514 et al.)

House Bill 5305 would provide that a pension or retirement benefit provided under the *County Board of Commissioners Act* would be subject to the proposed Act. (MCL 46.12a et al.)

House Bill 5306 would stipulate that a retirement board, retirement system, and a city, village, or municipality that is the custodian of funds of a retirement system under the *Fire Fighters and Police Officers Retirement Act* must comply with any applicable requirements under the proposed Act. Additionally, it would require that the amount appropriated by a municipality in a fiscal year be sufficient to pay the normal costs of any retirement health benefits provided by the retirement system in the amount required by the proposed Act (or as required under a corrective action plan under the proposed Act). (MCL 38.559)

⁴ House Fiscal Agency analysis: <http://www.legislature.mi.gov/documents/2015-2016/billanalysis/House/pdf/2015-HLA-6075-6163453F.pdf>

House Bill 5307 would amend the *Firemen and Policemen Pensions Act*. It would provide that certain interest payments from reserve funds allowed under the Act would be subject to the proposed Act. (MCL 38.571)

House Bill 5308 would provide that a retirement system established under the *City Library Employees' Retirement System Act* is subject to the proposed Act. (MCL 38.702)

House Bill 5309 would amend the *Optional Unified Form of County Government Act* to provide that a retirement system for the county's employees operating under the Act would be subject to the proposed Act. (MCL 45.554 et al.)

House Bill 5310 would add a Section 41a to the *Municipal Employees Retirement Act of 1984* that would allow a participating municipality to revoke its election to be governed by the provisions of the Municipal Employees Retirement System (MERS), for either all or a subset of its participating members. If a majority of the participating municipality's governing board votes to discontinue participation in MERS, the municipality must commission an actuarial analysis, which must include an analysis of the municipality's contribution requirements associated with revocation of participation. The participating municipality must select a methodology or amortization period, or both, to determine its contribution requirement, and must fund those contribution requirements. Finally, the retirement system may not require participation in another retirement plan as a condition for discontinuing participation. (MCL 38.1536 and proposed 38.1541a)

House Bill 5311 would amend the *Revised Municipal Finance Act* to accelerate the sunset of a provision allowing municipalities to issue municipal securities to cover the costs of their unfunded pension liability and unfunded accrued health care liability. The bill would move the sunset from December 31, 2018 to December 31, 2017. (MCL 141.2518)

House Bill 5312 would provide that the provisions of the *Open Meetings Act* would not apply to a financial management team (created by HB 5299) or the Local Government Retirement Stability Board (created by HB 5298). (MCL 15.263)

House Bill 5313 would stipulate that the provision of retirement benefits as part of a system of compensation by a city under the *Home Rule City Act* would be subject to the proposed Act. (MCL 117.4i and 117.4p; proposed MCL 117.4u)

Tie-bars

HB 5300 is tie-barred to HB 5299, meaning it could not take effect unless HB 5299 is also enacted. HBs 5301 to 5310 and 5313 are tie-barred to HB 5298.

BACKGROUND INFORMATION:

This bill package is understood to be based on recommendations from the Responsible Retirement Reform for Local Government Task Force, initiated by Governor Snyder and made up of 20 municipal, business, and union leaders from around the state. In July of

2017, the task force released its report, based around the following four main recommendations:

- Greater reporting and transparency must be required of all local units to ensure a full understanding of the size and scope of the problem, and where the biggest challenges exist. This includes reporting using uniform assumptions to allow for better comparisons.
- A pension and OPEB fiscal stress test system for local governments should be created to alert and assist local units in crafting solutions to best position them to continue to serve their residents, while funding their obligations and protecting benefits for employees and retirees. This system should identify and focus action on the local units experiencing the greatest fiscal stress.
- This system, along with the creation of a new Municipal Stability Board (MSB), should assist in the review of a local unit's finances and the development of a corrective action plan. The MSB should also provide research, training, and technical assistance.
- In addition to meeting existing constitutional and statutory requirements to pay pension costs, going forward all local governments should meet a minimum requirement to pay OPEB normal costs for new hires (i.e., to prefund new active employee's current year obligation), if offered.

The report noted that some task force members objected to the establishment of new funding requirements, as they felt the requirements would have too severe an impact on local units' ability to provide current services. Additionally, the report stated that members disagreed on the powers to be delegated to an MSB, with a majority believing that the role should be limited to making recommendations and providing technical support and a minority that "the MSB should be able to unilaterally impose changes if the local unit was unable to successfully implement a corrective action plan."

FISCAL IMPACT:

House Bill 5298

The bill could increase costs for local units of government depending on the extent to which the bill's pension and retiree health care funding requirements and actuarial assumptions and methods increased their required pension and OPEB contributions. Increased contributions, while raising costs initially, would likely create long-term savings because prefunding those costs allows a system to gain interest with which to pay the benefits in the future. However, the bill's waiver provisions could mitigate this impact for local governments for which this requirement would cause an undue hardship.

Prohibiting retiree health care for retirees and beneficiaries who are enrolled in or eligible for other comparable employer-sponsored health care would create savings for local units. However, the magnitude of savings would depend on the extent to which local

governments currently pay those costs for applicable retirees and the number of retirees to whom this might apply.

Creating an underfunded status for local units that must then create corrective action plans to avoid financial emergency status could create an incentive for local units to take measures that would increase retirement system payments, reduce benefit costs, or increase revenues in order to improve their retirement benefit systems' funded status. The fiscal impact would vary from one unit to the next depending on each unit's corrective action plan.

The bill would create costs for the state Department of Treasury related to the additional administrative requirements, including reviewing undue hardship waiver requests, summarizing local OPEB reports and making them available online, promulgating rules to establish standards for actuarial assumptions and other valuation methods, creating an evaluation system to provide for review and oversight of underfunded local units, and providing staff support to the Local Government Retirement Stability Board. However, the bill appropriates \$1.5 million GF/GP for FY 2017-18 for this purpose.

House Bill 5299

The bill could create an indeterminate fiscal impact for local units for which a financial emergency is determined to the extent that the financial management team takes actions to revise a local unit's budget to address its retirement benefit systems' funded status. The impact would depend on the specific remedies for each local unit.

The bill would create costs for the state Department of Treasury related to the additional administrative requirements, including paying for financial management team member compensation, providing staff support to the financial management team, and creating a website to allow residents to submit input. However, the bill appropriates \$250,000 GF/GP for FY 2017-18 for this purpose.

House Bill 5310

The bill could create savings for a local unit that no longer wanted to participate in MERS, assuming that the choice to leave was related to offering a reduced retirement benefit like a defined contribution plan, but the impact would depend on whether any, or what, benefit replaced the previous plan with MERS, and whether there were revised annual required contributions related to fully funding existing benefits if a plan were closed.

However, having to prepare for the possibility of large units or a significant number of MERS participants withdrawing from the plan would require MERS to maintain a much higher cash balance to avoid liquidity issues in paying monthly benefits. Shifting more funds to cash would decrease overall investment returns earned by the remaining participants. The investment returns for MERS participants also could diminish if MERS' purchasing power were significantly reduced.

House Bill 5311

The bill would have an indeterminate fiscal impact on any eligible local unit that had intended to issue or refinance a security or bond for all or a portion of its unfunded liabilities in 2018. The fiscal impact of bonding for unfunded liabilities depends on the funded status of a plan and the unit's ability to take advantage of borrowing rates relative to future retirement system investment returns. Bonding for those obligations creates a fixed debt, as opposed to retirement system contributions for unfunded liabilities, which increase or decrease as investment returns and other factors built into actuarial assumptions fluctuate over time.

ARGUMENTS:

For:

Mainly, proponents argue that their plan presents the best chance of preserving retirement benefits. By holding municipalities with underfunded systems accountable for funding those systems on a defined schedule, they argue, the plan would ensure that the benefits are available when retirees need them. Failure to act now would only exacerbate the problem; they state that it is the responsibility of the legislature to make tough choices now to prevent harsh cuts in the future.

Proponents argue that the 5 phases in the proposed Act provide a necessary structure for addressing the problem of underfunded retirement systems, while also allowing enough flexibility to meet the various needs of the many systems.

The plan would allow underfunded units to progress through phases 1-4, and to present their own corrective action plan, before the possibility of enforcement actions. If a local unit is unable to agree on a plan, or if the plan is deemed insufficient by the Local Government Retirement Stability Board, the Board could create a financial management team for the local unit. However, proponents argue that this possibility is only available as a last resort, and in order to give the plan the "teeth" it needs to ensure compliance. Without phase 5's possibility of a financial management team (and, if determined necessary by the team, an emergency manager), local units might continue as they have—increasingly falling further behind in funding their pension and OPEB obligations. Proponents ask: wouldn't a financial team, however unwelcome, be preferable to allowing a bankruptcy judge to cut benefits unilaterally?

Response:

Critics argue that there is little difference between a financial management team cutting benefits and a federal bankruptcy judge doing so. Additionally, they state that the unfunded status of a local unit's system would not result in bankruptcy, as the underfunding of a system would not necessarily lead to insolvency.

Against:

Opponents of the plan include organizations that represent more than 30,000 police and firefighters across the state of Michigan. Those professions are inherently dangerous, with health risks following retirees beyond their working years. They argue that, in many cases, police and firefighters made concessions during their working years based on the assurance

that their pension and health benefits were guaranteed after retirement. They expressed concern that the bill would codify a 2015 U.S. Supreme Court decision⁵ that, in order for collectively bargained retiree health care benefits to be vested for life, a plan must explicitly state as much.

Critics argued that the plan presents a one-size-fits-all solution, which would subject all of the approximately 900 retirement systems to the same scrutiny, regardless of their funding levels or the steps they have taken independently to address underfunding. Certain provisions of the plan, such as prohibiting new entrants into defined benefit systems, may make financial sense for underfunded systems, but may not be necessary for adequately funded systems, they argue. Why must those funded systems, which may seek to use enhanced benefits offerings to attract and retain talent, be limited simply because other units have underfunded systems?

Opponents repeatedly stated that the Responsible Retirement Reform for Local Government Task Force's recommendations were issued unanimously, and that they would support a plan based on those recommendations. Why, they ask, would the legislature advance a plan that departs from the recommendations at several critical junctures?

POSITIONS:

Representatives of the following organizations testified in support of HBs 5298-5313:

- Governor Snyder's administration (12-5-17)
- Retirement Security Initiative (12-5-17)
- Pension Integrity Project—Reason Foundation (12-5-17)
- National Federation of Independent Business (12-5-17)
- Michigan Chamber of Commerce (12-5-17)
- Business Leaders for Michigan (12-5-17)
- City of Port Huron (12-5-17)

A representative of the Grand Rapids Chamber and West Michigan Policy Forum testified in support of HBs 5298-5313 with amendments. (12-5-17)

The following organizations support HBs 5298-5313:

- Michigan Restaurant Association (12-5-17)

Representatives of the following organizations testified in opposition to HBs 5298-5313:

- Michigan Association of Chiefs of Police (12-5-17)
- Michigan Professional Firefighters Union (12-5-17)
- Michigan Sheriffs' Association (12-5-17)
- Police Officers Association of Michigan (12-5-17)
- Michigan Association of Fire Chiefs (12-5-17)
- Fraternal Order of Police (12-5-17)

⁵ *M&G Polymers USA, LLC v Tackett*, 574 US ___ (2015); https://www.supremecourt.gov/opinions/14pdf/13-1010_7k47.pdf

- Michigan Association of Police Organizations (12-5-17)
- Deputy Sheriff's Association of Michigan (12-5-17)
- Prosecuting Attorneys Association of Michigan (12-5-17)
- Michigan AFL-CIO (12-5-17)
- Michigan Association of Public Employee Retirement System (12-5-17)
- American Federation of State, County and Municipal Employees (12-5-17)

A representative of Grand Rapids Professional Firefighters Local 366 testified in opposition to HB 5298. (12-5-17)

Representatives of the following organizations testified in opposition to HBs 5298-5313 as introduced:

- Michigan Municipal League (12-5-17)
- Michigan Association of Counties (12-5-17)
- Michigan Townships Association (12-5-17)

A representative of the Municipal Employees Retirement System testified in opposition to HB 5310 as introduced. (12-5-17)

The following organizations oppose HBs 5298-5313:

- Northern Michigan Fire Chiefs Association (12-5-17)
- Southeast Michigan Fire Chiefs (12-5-17)
- AARP (12-5-17)
- County Roads Association of Michigan (12-5-17)
- Farmington Hills Fire Department (12-5-17)
- East Lansing Firefighters Local 1609 (12-5-17)
- Harrison Township Firefighters Michigan Professional Firefighters Union (12-5-17)
- Macomb Firefighters Local 5023 (12-5-17)
- Fraternal Order of Police Labor Council (12-5-17)
- Macomb County (12-5-17)
- St. Clair Shores Fire Department (12-5-17)
- Shelby Township Fire Department (12-5-17)
- Coalition for Secure Retirement-Michigan (12-5-17)

The Taylor Police Officers Labor Association opposes HBs 5300-5315. (12-5-17)

The following organizations oppose HB 5298:

- East Lansing Firefighters Local 1609 (12-5-17)
- Dearborn Police (12-5-17)
- City of Wayne Retirees (12-5-17)

Legislative Analyst: Jenny McInerney
Fiscal Analyst: Bethany Wicksall

■ 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.