



Senate Fiscal Agency  
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## BILL ANALYSIS



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Senate Bill 686 (Substitute S-4 as passed by the Senate)  
Senate Bill 688 (Substitute S-1 as passed by the Senate)  
Senate Bill 689 (as passed by the Senate)  
Senate Bill 690 (Substitute S-2 as passed by the Senate)  
Senate Bills 691 through 694 (as passed by the Senate)  
Senate Bill 695 (Substitute S-3 as passed by the Senate)  
Senate Bills 696, 697, and 698 (as passed by the Senate)  
Senate Bill 699 (Substitute S-1 as passed by the Senate)  
Sponsor: Senator Jim Stamas (S.B. 686, 690, 694, 696, & 698)  
Senator Mike Shirkey (S.B. 688, 689, 695, 697, & 699)  
Senator Dave Hildenbrand (S.B. 691)  
Senator Phil Pavlov (S.B. 692)  
Senator Dave Robertson (S.B. 693)  
Committee: Michigan Competitiveness

Date Completed: 12-11-17

**CONTENT**

**Senate Bill 686 (S-4) would enact the "Protecting Local Government Retirement and Benefits Act" to do the following:**

- **Require a local unit of government, beginning July 1, 2018, to pay normal costs (the cost of retirement health benefits as they are earned) for new employees and to pay retiree premiums due for retirants in its retirement system, if the local unit offered or provided an employee, or a former employee hired before the Act's effective date, with a retirement health benefit.**
- **Require the local unit to submit a summary retiree health care report annually to its governing body and the Department of Treasury.**
- **Require the local unit to have an actuarial experience study conducted by the plan actuary for each retirement system at least every five years.**
- **Require the local unit, at least every eight years, to have a peer actuarial audit conducted by an actuary who was not the plan actuary or to replace the plan actuary.**
- **Require the State Treasurer annually to establish uniform actuarial assumptions of retirement systems.**
- **Require a local unit annually to calculate the funded ratios of each retirement system using those assumptions and report to the Department of Treasury.**
- **Require the State Treasurer to create an evaluation system to identify and resolve the underfunded status of a local unit.**
- **Require the State Treasurer each to determine the underfunded status of every local unit of government each year, and to provide for oversight of an underfunded local unit.**
- **Provide that a local unit would be underfunded if the actuarial accrued liability of a retirement health system were less than 40% funded and, in the case of a city, village, township, or county, the annual required contribution for all of its**

retirement health systems were more than 12% of its general fund operating revenue.

- Provide that a local unit would be underfunded if the actuarial accrued liability of a retirement pension system were less than 60% funded and, in the case of a city, village, township, or county, the annual required contribution for all of its retirement pension systems were more than 10% of its general fund operating revenue.
- Provide that a local unit would be underfunded if it did not make its normal cost or retiree premium payments, or if it had not reported the annual cost of the liability of the retirement health system or pension system using the uniform actuarial assumptions.
- Require the State Treasurer to waive a determination of a local unit's underfunded status if the local unit were adequately addressing it, and require the Treasurer to take certain steps if a waiver were not granted.
- Create the Municipal Stability Board in the Department of Treasury, and require a local unit in underfunded status to submit a corrective action plan to the Board for its approval.
- Require the Board to notify a local unit if the Board disapproved a corrective action plan, and require the local unit to resubmit the plan within 60 days.
- List corrective options that a corrective action plan could include.
- Require the Board to monitor each underfunded local unit's compliance with the proposed Act and its corrective action plan.
- Require the Board to notify a local unit that was not in substantial compliance, and require the local unit to address the determination of noncompliance within 60 days.
- Require the State Treasurer to post on the Department's website the uniform actuarial assumptions, a summary of local units' reports, the underfunded status of each local unit, the waiver status of local units, and approved corrective action plans.
- Require a local unit to post the same information that applied to it.

**Senate Bill 688 (S-1)** would amend the Public Employee Retirement System Investment Act to delete provisions requiring a system to post an informational report outlining the steps it may be taking to decrease its unfunded actuarial accrued liability, if the system's actuarial accrued liability for retiree health or pension is not at least 60% funded.

**Senate Bill 689** would amend Public Act 293 of 1966, which governs charter counties, to:

- Specify that if a county provided a system of retirement for its officers and employees under the Act, the system would be subject to the proposed Protecting Local Government Retirement and Benefits Act.
- Delete a provision under which the county board of commissioners, in a county with a population of 600,000 or more, may have up to 27, rather than 21, members.

**Senate Bill 690 (S-1)** would amend the Municipal Employees Retirement Act to make the powers and duties of the Municipal Employees Retirement System retirement board subject to the proposed Act.

**Senate Bill 691** would amend Public Act 156 of 1851, which governs county boards of commissioners and allows counties to create pension plans for their employees, to specify that a pension or retirement benefit under the Act would be subject to the proposed Protecting Local Government Retirement and Benefits Act.

**Senate Bill 692** would amend Public Act 139 of 1973, which provides for an optional unified form of county government, to specify that, for a county that had adopted such a form of government and provided for a retirement system for the county's employees, the retirement system would be subject to the proposed Act.

**Senate Bill 693** would amend Public Act 339 of 1927, which provides for a retirement system for public library employees, to specify that a retirement system established under the Act would be subject to the proposed Act.

**Senate Bill 694** would amend Public Act 28 of 1966, which allows the board of trustees of various local retirement systems to increase benefits, to make a provision of the Act subject to the Protecting Local Government Retirement and Benefits Act. That provision allows a retirement system board of trustees, with approval of the local unit's governing body, to use up to half of the interest earned by any reserve fund in the system to contract for medical, hospital, or nursing care for any person receiving benefits from the system.

**Senate Bill 695 (S-3)** would amend the Fire Fighters and Police Officers Retirement Act to provide that a retirement board under the Act, a retirement system under the Act, and city, village, or municipality that was the custodian of a retirement system's funds under the Act, would have to comply with the proposed Act.

**Senate Bill 696** would amend Chapter 16 of the Revised Statutes of 1846, which provides for the powers and duties of townships, to make various powers of a township, including the authority to establish an employee retirement system, subject to the proposed Act.

**Senate Bill 697** would amend the Home Rule City Act to specify that, if a city provided retirement benefits as part of a system of compensation, those benefits would be subject to the Protecting Local Government Retirement and Benefits Act.

**Senate Bill 698** would amend the Reciprocal Retirement Act to require a reciprocal unit and a reciprocal retirement system to comply with applicable requirements of the proposed Act.

**Senate Bill 699 (S-1)** would amend Public Act 566 of 1978, which prohibits a public officer from holding incompatible offices, to specify that the prohibition would not apply to a member of the Municipal Stability Board created under the proposed Act.

Senate Bills 688 (S-1) through 699 (S-1) are tie-barred to Senate Bill 686.

Senate Bills 686 (S-4) and 688 (S-1) are described in more detail below.

#### **Senate Bill 686 (S-4)**

##### Legislative Finding & Declaration

The proposed Protecting Local Government Retirement and Benefits Act states, "The legislature finds and declares that this act is intended to reflect the July 2017 Report of Findings and Recommendations for Action of the Responsible Retirement Reform for Local Government Task Force."

## Definitions

The Act would define "local unit of government" as any of the following:

- A city.
- A village.
- A township.
- A county.
- A county road commission.
- A public airport authority created under the Aeronautics Code
- A metropolitan government or authority established by the Legislature under the State Constitution.
- A metropolitan district created under the Metropolitan District Act (which allows two or more cities, townships, and/or villages to create metropolitan districts for various purposes).
- An authority created under Public Act 147 of 1939 (which established the Huron-Clinton Metropolitan Authority).
- A municipal electric utility system as defined in the Michigan Energy Employment Act.
- A district, authority, commission, public body, or public body corporate created by one or more of the entities listed above.

"Retirement system" would mean a retirement system, trust, plan, or reserve fund that a local unit of government establishes, maintains, or participates in and that, by its express terms or as a result of surrounding circumstances, provides retirement pension benefits or retirement health benefits, or both.

"Retirement health benefit" would mean an annuity, allowance, payment, or contribution to, for, or on behalf of a former employee or a dependent of a former employee to pay for any of the following components:

- Expenses related to medical, drugs, dental, hearing, or vision care.
- Premiums for insurance covering medical, drugs, dental, hearing, or vision care.
- Expenses or premiums for life, disability, long-term care, or similar welfare benefits for a former employee.

"Retirement pension benefit" would mean an allowance, right, accrued right, or other pension benefit payable under a defined benefit pension plan to a participant in the plan or a beneficiary of the participant.

## Retiree Health Benefits

Beginning July 1, 2018, if a local unit of government offered or provided an employee of the local unit, or a former employee first employed by the local unit before the effective date of the proposed Act, with a retirement health benefit, the local unit would be subject to all of the provisions described below.

Normal Cost & Premium Payments. The local unit would have to pay at least both of the following:

- Normal costs for employees first hired after June 30, 2018.
- Retiree premiums that were due for retirants in the retirement system

("Normal cost" would mean 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.)

Retiree Health Care Report. The local unit annually would have to electronically submit a summary retiree health care report in a form prescribed by the Department of Treasury to its governing body and the Department within six months after the local unit's fiscal year ended. The Department would have to post on its website an executive summary of each report submitted to the Department, and include in the executive summary the applicable system's unfunded actuarial accrued liability (UAAL). The Department also would have to submit each executive summary to the Senate and House of Representatives Appropriations Committees and Fiscal Agencies within 30 days after the posting.

"Summary retiree health care report" would mean a report that includes all of the following for each retirement system of the local unit that provides retirement health benefits:

- The name of the system and the names of its investment system and service providers.
- The system's assets and liabilities and changes in net plan assets on a plan-year basis.
- The system's funded ratio based on the ratio of valuation assets to actuarial accrued liabilities on a plan-year basis.
- The assumed rate of return of the system.
- The actual rate of return of the system for the previous one-year, five-year, and 10-year periods.
- The discount rate used by the system.
- The system's amortization method for unfunded liability, indicating whether it is open or closed.
- The system's amortization method, indicating whether it is level percent or level dollar, and the assumed payroll growth rate.
- The system's remaining amortization time period.
- The annual required contribution for the system, indicating the normal cost and the amortization payment toward the UAAL.
- The retirement system's health care inflation assumption.
- The number of active employees and retirants in the system.
- The amount of premiums paid on behalf of retirants in the system.

Actuarial Experience Study & Actuarial Audit. At least every five years, the local unit would have to have an actuarial experience study conducted by the plan actuary for each retirement system of the local unit.

At least every eight years, the local unit would have to do one or both of the following:

- Have a peer actuarial audit conducted by an actuary that was not the plan actuary.
- Replace the plan actuary.

A local unit would be exempt from these requirements if it were eligible to use a specified alternative measurement method under Government Accounting Standards Board (GASB) standards.

#### Retirement System Actuarial Assumptions; Annual Report

The State Treasurer annually would be required to establish uniform actuarial assumptions of retirement systems, including investment returns, salary increase rates, mortality tables, discount rates, and health care inflation.

On an annual basis, a local unit of government would have to electronically submit a report in a form prescribed by the Department to the governing body of the local unit and to the

Department, within six months after the end of the local unit's fiscal year. For purposes of the report, a local unit annually would have to calculate the funded ratios of each retirement system of the local unit using the uniform actuarial assumptions established by the State Treasurer.

#### Underfunded Status Determination

The State Treasurer would be required to create an evaluation system (a system to provide for the identification of, and a corrective action plan to resolve, the underfunded status of a local unit of government).

Each year beginning after December 31, 2017, the State Treasurer would have to determine the underfunded status of each local unit of government. Beginning on the effective date of that determination, the Treasurer would have to provide for review and oversight of the local unit.

The State Treasurer would have to determine that a local unit was in underfunded status if the actuarial accrued liability of a retirement health system of the local unit were less than 40% funded, according to the most recent annual report, and, if the local unit were a city, village, township, or county, the annual required contribution for all of the retirement health systems of the local unit were greater than 12% of its annual general fund operating revenue, based on the most recent fiscal year.

The State Treasurer also would have to determine that a local unit was in underfunded status if the actuarial accrued liability of a retirement pension system of the local unit were less than 60% funded, according to the most recent annual report, and, if the local unit were a city, village, township, or county, the annual required contribution for all of the retirement pension systems of the local unit were greater than 10% of its annual general fund operating revenue, based on the most recent fiscal year.

In addition, the State Treasurer would have to determine that a local unit was in underfunded status if either of the following applied:

- The local unit had not reported the annual cost of the liability of the retirement health system or retirement pension system using the uniform actuarial assumptions established by the Treasurer.
- The local unit failed to make the required payments for normal costs for new employees, and for retiree premiums due for retirants in the retirement system.

("Annual report" would mean the most recent audited financial statement reporting a local unit of government's liability for retirement pension benefits and retirement health benefits as determined under applicable government accounting standards of the GASB.)

#### Waiver of Underfunded Status Determination; Treasury Requirements

To qualify for a waiver of an underfunded status determination, a local unit of government's administrative officer and governing body would have to approve a plan demonstrating that the underfunded status was being addressed, and approve a waiver application. The State Treasurer would have to issue a waiver of the determination of underfunded status for a local unit if he or she determined that the local unit was adequately addressing the underfunded status.

For any underfunded local unit that was not granted a waiver, the Department would have to do all of the following:

- Undertake an individualized and comprehensive internal review of the local unit's retirement system.
- Discuss changes or reforms that had been made with the local unit's designated officials.
- Review actuarial projections, including trends and projections.

### Municipal Stability Board

The Board would be created within the Department of Treasury and, except as otherwise provided in the Act, would have to exercise its powers, duties, and functions independently of the State Treasurer. The Board would consist of three members appointed by the Governor. Each member would have to be a resident of the State with knowledge, skill, or experience in accounting, actuarial science, retirement systems, retirement health benefits, or government finance. One member would have to represent State officials, one would have to represent local officials, and one would have to represent employees and retirees.

The Board would have to meet at least quarterly. Board members would have to serve without compensation but could receive reimbursement for travel and expenses incurred in the discharge of official duties. The Board could contract for professional services.

The Board would be required to review and annually update a list of best practices and strategies that would assist an underfunded local unit in developing a corrective action plan.

The validity of the Board would be conclusively presumed unless questioned in an original action filed in the Court of Claims within 60 days after the effective date of the proposed Act.

### Corrective Action Plan

An underfunded local unit of government would have to develop and submit for approval a corrective action plan based on what the local unit determined as the best components of a plan for it.

The Board would be required to review and vote on the approval of a corrective action plan submitted by a local unit. A local unit that was in underfunded status would have to submit a corrective action plan to the Board within 180 days after the determination of that status. The Board could extend that deadline by up to 45 days if the local unit submitted a reasonable draft of a corrective action plan and requested an extension.

The governing body of the local unit would have to approve the plan before submitting it to the Board. The Board would have to review or reject the plan within 45 days after it was submitted.

A corrective action plan could include the corrective options for correcting underfunded status (as set forth below) and any additional solutions to assist with reducing annual expenses or improving funding levels related to underfunded status to maintain and preserve retirement pension benefits and retirement health benefits. A local unit also could include in its plan a review of the local unit's budget and finances.

The Board could review the inclusion of the corrective options and additional solutions as part of its approval criteria to determine whether a corrective action plan was designed to permanently remove the local unit from underfunded status.

If the Board voted to disapprove a corrective action plan that had been submitted, within 15 days the Board would have to notify the local unit and provide a report detailing the reasons for the disapproval. The local unit would have 60 days to address those reasons and resubmit a plan for approval.

A local unit would have up to 180 days after approval of a corrective action plan to implement the plan to achieve the necessary cost reductions and funding improvements to permanently correct its underfunded status.

The Board would have to monitor each underfunded local unit's compliance with the Act and any corrective action plan. The Board would have to adopt a schedule, not less than every two years, to certify that the local unit was in substantial compliance with the Act. If the Board determined that a local unit was not in substantial compliance, with 15 days the Board would have to provide a notification and report to the local unit detailing the reasons for that determination. The local unit would have 60 days to address the determination.

### Corrective Options

A corrective action plan could include the development and implementation of corrective options for the local unit to address and permanently resolve its underfunded status.

For retirement pension benefits, corrective options could include any of the following:

- Closing the current defined benefit plan.
- Implementing a multiplier limit.
- Reducing or eliminating new accrued benefits.
- Implementing final average compensation standards.

For retirement health benefits, corrective options could include the following:

- Requiring cost sharing of premiums and sufficient copays.
- Capping employer costs.

### Posting Requirements

The State Treasurer would have to post all of the following on the Department's website:

- The uniform actuarial assumptions established by the Treasurer.
- A summary report of the reports submitted by local units, calculating the funded ratios of each retirement system using the actuarial assumptions.
- The underfunded status of local units.
- The current waiver status of local units.
- Any approved corrective action plan.

A local unit of government would have to post on its website, or in a public place if it did not have a website, the information described above that applied to the local unit.

## **Senate Bill 688 (S-1)**

The Public Employee Retirement System Investment Act codifies the investment authority of State and local public employee retirement systems, and defines and limits the amount and type of investments that may be made by those acting as an investment fiduciary (typically, the applicable retirement board) on behalf of a retirement system.

For a system other than a State unit, if the system's actuarial accrued liability for retiree health care or pension is not at least 60% funded according to the most recent summary annual report, the system must post an informational report on its website outlining the steps, if any, the system may be taking to decrease its unfunded actuarial accrued liability. If a system does not have a website, the political subdivision sponsoring the system must make these steps available to plan participants and beneficiaries, as well as the residents of the



political subdivision. The system also must submit to the Department of Treasury the steps the system may be taking to decrease its UAAL.

The bill would delete those requirements.

The Act requires an investment fiduciary to publish a summary annual report and lists the information that the report must contain. For a system other than a State unit, the investment fiduciary must submit the summary annual report to the Department of Treasury not less than 30 days after publication.

The Department must post on its website an executive summary of each summary annual report submitted to it. The executive summary must include the applicable system's unfunded actuarial accrued liability for retiree health care and pension. The bill would delete the reference to health care.

(A State unit is a system established under the State Employees' Retirement Act, the Public School Employees Retirement Act, the Judges Retirement Act, and the State Police Retirement Act.)

MCL 38.1133 & 38.1140h (S.B. 688)  
MCL 45.514 et al. (S.B. 689)  
MCL 38.1536 (S.B. 690)  
MCL 46.12a et al. (S.B. 691)  
MCL 45.554a et al. (S.B. 692)  
MCL 38.702 (S.B. 693)  
MCL 38.571 (S.B. 694)  
Proposed MCL 38.552a. (S.B. 695)  
MCL 41.110b (S.B. 696)  
MCL 117.4i et al. (S.B. 697)  
Proposed MCL 38.1102a (S.B. 698)  
MCL 15.183 (S.B. 699)

Legislative Analyst: Suzanne Lowe

## **FISCAL IMPACT**

### **Senate Bill 686 (S-4)**

#### State

Senate Bill 686 (S-4) likely would increase costs to the State in the Department of Treasury. Under the bill, the Department could experience increased costs related to annually establishing uniform actuarial assumptions, creating an evaluation system, and providing for comprehensive review and oversight of local governments' funded status. In addition, the creation and operations of the Municipal Stability Board could increase costs to the Department, particularly if the Board were to contract for professional services, and for reimbursement of travel and expenses.

For context, the existing Financial Independence Team in the Department, which reviews school district finances, has 9.0 full-time equated positions and a fiscal year 2017-18 General Fund/General Purpose appropriation of \$4.2 million. There are roughly 900 school districts, charter schools, and intermediate districts that submit financial data to the Department under the early warning system. There are roughly 1,800 local units of government that would be required, under the bill, to submit annual summary pension and retiree health care reports to the Department for review.

## Overview of Funding Pensions and Retiree Health Care

Under the State Constitution (Article IX, Section 24), pension plans are required to be prefunded, and the annual prefunding payment for a pension is called the normal cost. The normal cost represents the amount of money necessary to be contributed in a given year to pay for that year's benefits that are earned. If that money is invested, and all of the actuarial assumptions are met, that year's worth of normal cost contributions will grow over time with investment earnings and then pay for that year's worth of pension payments in the future.

However, if actual experience differs from the assumptions in a negative manner (e.g., the stock market does not earn the assumed rate of return, or benefits are paid for a longer period of time due to people living longer than assumed), a shortfall can occur in the assets funding the plan. That shortfall is called the unfunded actuarial accrued liability (UAAL). The UAAL represents the shortfall in assets necessary to pay for benefits earned in the past. Another way to think of the UAAL is like a home mortgage; however, the mortgage is not necessarily a fixed amount and can change based on actual experience in a given year compared to assumptions. For systems with funding shortfalls, an annual UAAL payment should be made, along with the normal cost payment.

Prefunding is not currently required for retiree health care plans. Local units offering retiree health care may choose to prefund (which means putting money aside now so that it can generate investment earnings to help defray retiree costs in the future), or may choose to pay the costs as they arise (e.g., pay-as-you-go). The latter costs more on a long-term basis due to the foregoing of investment earnings.

### Local

The bill would have an indeterminate fiscal impact on local units of government. Senate Bill 686 (S-4) would mandate minimum normal cost contributions for retiree health plans for employees newly hired after June 30, 2018, as well as the payment of retiree premiums due for retirees. In addition, the bill's requirement to submit annually a summary retiree health care report could impose some additional slight cost on local units of government; however, it is likely that most already prepare such a report, so there should be little to no cost in those situations. The requirements to have an actuarial experience study at least every five years, and a peer actuarial audit at least every eight years, also could impose some additional costs on a local unit not already doing these activities.

For local units of government not already following at least the prescribed contribution levels for retiree health care, there would be an increase in costs in the short run, with likely reductions in costs in the long run. Contributions made today are assumed to grow over time as those contributions are invested and earn a rate of return. The more dollars that were invested today through the required normal cost contributions (if a local unit is not already making these contributions), the more time those dollars would have to grow and be used to pay the cost of benefits down the line.

Local units determined to be underfunded could experience an indeterminate fiscal impact related to the requirements to develop, submit, and implement a corrective action plan. There could be some slight costs associated with the actual development of the plan, and, depending on the extent to which a local unit followed and implemented an approved plan, as well as what the plan contained in terms of cost reductions and funding improvements of pension or retiree health care plans, there could be either costs or savings to the local unit. The bill specifies that a local unit would have up to 180 days after approval of a corrective action plan to begin implementation. If a local unit were determined to be in noncompliance with its corrective action plan, it would have 60 days from the notification of noncompliance to address that determination.

**Senate Bills 688 (S-1) through 699 (S-1)**

The bills would amend various acts to require compliance with Senate Bill 686 (S-4), and as such would not have an independent fiscal impact.

Fiscal Analyst: Kathryn Summers

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.