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STATE TREASURER TO MANAGE DEFERRED COMP. SYSTEM

House Bill 4941 with committee amendment
First Analysis (10-31-95)

Sponsor: Rep. Kim Rhead
Committee: Appropriations

THE APPARENT PROBLEM:

Public Act 306 of 1976 authorizes the Department of Civil Service to provide for the administration and investment of the state deferred compensation system, a program that enables state employees to direct a portion of their earnings, untaxed, into an investment program to be withdrawn later (presumably, at retirement) when the amounts may be taxed at a lower rate. At present, the state provides its employees two options for deferring a portion of their earnings into an investment program--known as the Plan I 457 and Plan II 401(K). Both of these plans offer a "fixed" investment choice, in which money is invested in what are known as "guaranteed investment contracts," or GICs, entered into with various life insurance companies. GICs tend to be less risky than stocks, but also provide a lower return on investments. Employees also may choose from among different mutual funds, which invest in stocks, bonds, government securities, and short-term money market instruments, offered through certain mutual fund companies.

The Secchia Commission, formed in 1991 to suggest ways to improve efficiency in state government, recommended transferring responsibility for administration of the deferred compensation program from the Department of Civil Service to the Department of Treasury, which oversees investment of the state's general fund assets. In addition, a recent auditor general review of the treasury department's internal procedures for making investment decisions recommended a number of changes that recently were implemented. These procedures, some believe, could have helped prevent a loss incurred by the deferred compensation system--the total amount of which is not yet known--when a Canadian life insurance company with which the state had approximately $100 million of its fixed investment portfolio invested under a GIC declared bankruptcy in 1994. To ensure investment decisions are made according to a strict internal control process, legislation has been proposed to transfer administrative and investment responsibilities for the deferred compensation program from the civil service department to the state treasurer.

THE CONTENT OF THE BILL:

The bill would amend Public Act 306 of 1976 to specify that, by October 1, 1996, the state treasurer would be responsible for the administration and investment of the state deferred compensation system.

MCL 38.1151

FISCAL IMPLICATIONS:

The House Fiscal Agency says the bill would not have fiscal implications for either the state or its local governments. (10-17-95)

ARGUMENTS:

For:

Back in the early 1970s, when the state began offering its employees the option of setting aside a portion of their present earnings, tax-free, into investments that could be tapped later, the legislature gave the Department of Civil Service authority to decide how the deferred compensation program would be invested since it already administered the state's payroll system. With this authority, the department decides such things as which mutual fund companies to contract with and which mutual fund groups employees may invest in. The department, however, also decides how to invest that portion of the deferred compensation program known as fixed investment funds, which are composed of guaranteed investment contracts, or GICs, entered into with the largest life insurance companies in the U.S. and Canada. Currently, the system's fixed investment portfolio has assets of approximately $1 billion. In 1994, however, a Canadian life insurance company with which the department entered into a GIC involving about $100 million failed. Consequently, the state probably will lose a portion of this investment in ensuing bankruptcy proceedings. Ironically, before this problem arose the Secchia Commission in 1991 recommended transferring responsibility for administration of the deferred compensation program from civil service to the treasury department, primarily to reduce government inefficiency when two different departments perform a similar function. As investment of the state's assets is one of the treasury department's primary functions, it only makes sense that it should oversee investment of the state's deferred compensation portfolio. Moreover, recent changes made to this department's internal control procedures over investment decisions should help steer the state away from potentially bad investments involving its deferred compensation fixed-investment portfolio.

POSITIONS:

The Department of Treasury does not oppose the bill. (10-25-95)

The Department of Civil Service does not oppose the bill. (10-26-95)

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