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BILL ANALYSIS

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Senate Bill 1064 (Substitute S-1 as reported)
Sponsor: Senator Glenn D. Steil
Committee: Appropriations

CONTENT

The bill would amend Public Act 314 of 1965. The Act provides for the authorization of and limitations on the investment of assets of public employee retirement systems in Michigan. The bill proposes to name Public Act 314 of 1965 the "Public Employee Retirement System Investment Act". The amendments contained in Senate Bill 1064 (S-1) are generally designed to update the provisions of the Act to conform to the investment options currently available to large institutional investors.

The provisions of Public Act 314 of 1965 apply to all retirement systems operated by State or local governmental organizations in Michigan. There are currently more than 500 retirement systems subject to the provisions of the Act. The largest systems that must conform to the Act are the Public School Employees Retirement System and the State Employees Retirement System, which have combined assets valued in excess of $25.0 billion.

Senate Bill 1064 (S-1) proposes to make the following changes to Public Act 314 of 1965:

-- Amend the definitions section of the Act to include new definitions of “derivative”, “foreign security”, “investment grade”, and “investment fiduciary”, among others.
-- Amend the definition of how pension funds value “assets” from a cost basis to a market basis. This change is in conformance with new governmental accounting requirements.
-- Require that an investment fiduciary be a registered security dealer, a bank, or an insurance company.
-- Clarify that the limits placed on an investment fiduciary do not apply to pension funds in a defined contribution plan in which the participants direct the investment of the assets in their accounts.
-- Place general limits on the actions of an investment fiduciary in terms of acceptable ethical behavior.
-- Increase the maximum amount of a retirement system asset that may be invested in equity stocks from 60% to 65%.
-- Remove the limitation that excludes investments in the stock of a company that has not paid a dividend to shareholders in at least three of the past five years.
-- Increase the minimum size asset holding that a mutual fund trading company must manage from $100 million to $500 million before that mutual fund company is eligible to receive pension fund investments. The same asset level also would apply to investments in insurance companies.
-- Provide for the authorization to invest in obligations issued in the United States by foreign governments, banks, or corporations.
-- Prohibit foreign investments in countries that are identified by the United States State Department as engaging in or sponsoring terrorism.
-- Place limits on investments to ensure that no more than 5% of a pension system's assets are invested in one company and ensure that the total investment of a pension system does not exceed 5% of the valuation of an individual company.

-- Provide for the authorization to invest up to 5% of a pension system's assets in indirect real estate investment trusts.
-- Decrease the minimum asset size requirement of a retirement system that may invest in direct real estate investments from $250 million to $100 million in assets. These real estate investments are limited to 5% of the retirement systems' total assets.
-- Amend the provisions that currently allow pension systems with an asset valuation of between $10 million and $250 million to invest up to 5% of the system's assets in investments not specified in the Act. The amendment would allow all systems with assets under $250 million to utilize this 5% exclusion rule.
-- Provide that a system could invest up to 15% of the system assets in derivative type investments. The language on derivative investments would prohibit the investment of any pension funds in derivative investments that have the purpose of leveraging as a means of investments. (Derivative type investments are sophisticated financial instruments that derive their value from an underlying asset or index. Derivatives come in many forms such as futures, options, swaps, collaterized mortgage obligations and forwards.)
-- Provide that a pension system could not invest more than 20% of the system's assets in foreign securities.
-- Provide that a record, material, or other data received and used by an investment fiduciary in connection with the investment of assets that deals with proprietary information pertaining to the company in which the investment is being made would be excluded from provisions of the Freedom of Information Act (Public Act 442 of 1976). This exclusion applies to information that has not been publicly disseminated by the company and whose dissemination would cause the company a competitive disadvantage.

MCL 38.1132 et al.

FISCAL IMPACT

Senate Bill 1064 (S-1) provides for a general rewrite and update in the pension investment law to conform to the investment options currently available to large investors. The fiscal impact of the bill on the valuation of pension assets is unknown. This will depend on the quality of the investment decisions that are made on behalf of each pension fund.

Date Completed: 11-14-96 Fiscal Analyst: G. Olson

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