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PUBLIC EMPLOYEE HEALTH CARE FUNDS

Senate Bill 587 (Substitute H-1)
First Analysis (10-12-99)

Sponsor: Sen. Bill Bullard, Jr.
House Committee: Local Government and Urban Policy
Senate Committee: Local, Urban and State Affairs

THE APPARENT PROBLEM:

The Public Employee Retirement System Investment Act, originally enacted in 1965, authorizes state and local governments to invest the assets of their public employee retirement systems in stocks, bonds, and other obligations, as specified in the act. Amendments to the act have brought it up to date with current investment practices. Most recently, Public Act 485 of 1996 amended the Public Employee Retirement System Investment Act to establish guidelines for investing public pension system assets; to allow a greater percentage of retirement system assets to be invested in stocks; and, to expand the types of investments that may be made with retirement system assets.

While the act permits the investment of funds of a public employee retirement system in order to provide retirement benefits, state law does not authorize the investment of funds in the stock market to pay for retiree health care benefits. To help meet the rising cost of these benefits, it has been suggested that local governments be permitted to establish public employee health care funds and then to direct the funds'assets into investment opportunities, including stocks, that currently are available for public pension system assets.

THE CONTENT OF THE BILL:

The bill would create the Public Employee Health Care Fund Investment Act to permit the legislative body of a public corporation (a county, city, village, township, authority, district, board, or commission) to adopt a resolution establishing a public employee health care fund for the purpose of accumulating funds to provide for the funding of health care benefits to retirants and beneficiaries of the retirants of the public corporation. ("Fund" would be defined to mean a public employee health care fund created pursuant to this act and used for the accumulation and investment of funds for the purpose of funding health care for retired employees of the public corporation.)

Under the bill, money for the payment of health care benefits for retired employees of the public corporation could, at the discretion of the public corporation, be provided from this fund or any other fund or trust. ("Trust" would be defined to mean a trust created under the authority of a state or federal law for the purpose of funding retiree health care benefits.)

The bill specifies that the resolution to establish the fund would have to include all of the following:

--The designation of a person or persons who would act as the fund's investment fiduciary. ("Investment fiduciary" would mean a person or persons who exercised any discretionary authority or control in the investment of the fund's or trust's assets, and/or rendered investment advice to a fund or trust for a fee or other direct or indirect compensation.)

--A restriction of withdrawals from the fund solely for the payment of health care benefits on behalf of qualified persons and the payment of the fund's administrative expenses.

--The designation of who was a qualified person for payment of health care benefits from the fund. ("Qualified person" would mean a person or group of persons who are eligible to receive health care benefits and who are designated as a qualified person by the public corporation.)

--A determination of whether the fund would be established on an actuarial basis.

Under the bill, the investment fiduciary would be required to invest the assets of the fund in accordance with an investment policy adopted by the governing body of a public corporation, and in compliance with the Public Employee Retirement System Investment Act. However, the investment fiduciary would be required to discharge his or her duties solely in the interest of the public corporation. The corporation would be allowed to invest the fund's assets in the instruments and subject to the limitations governing the investment of assets under the Public Employee Retirement Systems Act.

Further, the legislative body of a public corporation could, by resolution, allow a trust to invest the assets of the trust in accordance with the Public Employee Retirement System Investment Act. In this instance, the resolution would be required to include: a statement of the authority under which the trust is established; and, approval to invest the assets of the trust in accordance with the Public Employee Retirement System Investment Act.

Finally, the bill specifies that the investment fiduciary would be required to have an actuarial review of the fund or trust prepared at least every five years, with assets valued on a market related basis. The investment fiduciary also would be required to prepare and issue a summary annual report to the legislative body of the public corporation that established the fund or trust.

HOUSE COMMITTEE ACTION:

The House Committee on Local Government and Urban Policy adopted a substitute for the bill. The substitute removed a provision from the bill that specified that once an actuarially-based fund was over funded by 110 percent or more, the local government would have been free to withdraw the excess from the fund, and invest the resulting savings elsewhere. The elimination of this provision, the re-definition of "fiduciary," and the clarification that the fund and its investments can be used solely for the provision of health care benefits to qualified persons, is said to bring the substitute bill into line with rules of the Internal Revenue Service regarding the administration of trusts that provide benefits to retirees.

FISCAL IMPLICATIONS:

According to the House and Senate Fiscal Agencies, the bill would have no fiscal impact on state government. Further, data are not available to determine accurately the local fiscal impact. SFA (8-4-99) HFA (9-28-99)

ARGUMENTS:

For:

As the cost of providing retiree health care benefits increases, communities are looking for ways to generate more funds to pay for future costs of these benefits. Public Act 20 of 1943 permits a local government to invest its funds in U.S. government bonds and securities, certificates of deposit, savings accounts, and certain other investment instruments that tend to produce short-term returns. Public Act 20, however, does not permit local governments to invest funds in the stock market, which is the type of long-term investing that could best offset the inflationary costs of health care benefits. Furthermore, Article 9, Section 19 of the State Constitution prohibits the state (and, by extension, local units of government) from investing in stock, " . . . except that funds accumulated to provide retirement or pension benefits for public officials and employees may be invested as provided by law . . . ". Consistent with the Constitution, the Public Employee Retirement System Investment Act provides statutory authority for the state and local units to invest retirement funds in the stock market (and other investment options) in order to fund pension benefits. Similarly, the bill would permit a local government to create a separate fund for retiree health care and to invest this money in accordance with the investment provisions of Retirement System Investment Act.

For:

In the form that the bill passed the Senate, some expressed concern that the bill provided an unintentional but nonetheless alluring incentive for a local government to reduce the benefits offered under a current retiree health care plan, since once a new actuarially-based fund was over-funded by 110 percent or more, the local government would have been free to revert money from the fund, and invest the resulting cost savings elsewhere. However, the substitute bill adopted by the House committee has eliminated this provision. The substitute bill requires that the fund and its investment be used solely for the payment of health care benefits on behalf of qualified people, and for the payment of the expenses of administration of the fund; defines "fiduciary"; and distinguishes funds from trusts, in accord with IRS rules. Consequently, the substitute bill would not affect the level of health care benefits being provided to retirees. Rather, the bill would allow (but not require) a community to set money aside in a separate fund to be invested and used to pay for retiree health care benefits, which could help defray the taxpayer cost of providing these benefits which often increase in cost more than 10 percent each year.

POSITIONS:

The Michigan Association of Public Employee Retirement Systems (MAPERS) is neutral on the bill but satisfied with changes made to this point. (9-30-99)

The Michigan Municipal League supports the bill. (9-30-99)

The Municipal Finance Officers Association supports the bill. (9-30-99)

The Michigan Townships Association supports the bill. (9-30-99)

Analyst: J. Hunault

■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.