



**House
Legislative
Analysis
Section**

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**VETERANS' TRUST FUND: EXPAND
INVESTMENT OPTIONS**

**Senate Bill 797 as introduced
First Analysis (1-9-02)**

**Sponsor: Sen. Valde Garcia
House Committee: Veterans Affairs
Senate Committee: Appropriations**

THE APPARENT PROBLEM:

The Michigan Veterans' Trust Fund (MVTF) was created by Public Act 9 of 1946 and initially funded by a post-war reserve fund that had been established in 1943 to assist veterans and their widows and dependents. Public Act 9 names the state treasurer as the custodian of the MVTF, but it gives full power to direct the investment of the trust fund in bonds or other governmental obligations to the State Administrative Board. However, House Joint Resolution H, approved by the voters in the 1996 general election, amended the constitution to establish the MVTF within the Department of Treasury and to charge the state treasurer with responsibility both for directing investment of the MVTF and for crediting interest and earnings of the fund to the fund. Thus, although statute still gives the authority to direct investment of the fund to the State Administrative Board, the constitution gives the authority to the state treasurer, who currently does direct fund investment.

Public Act 9 originally required—and currently requires—that \$50 million be held in trust and that expenses be paid out of any surplus and earnings from that amount. The act limits investments of fund money to bonds and various other government debt instruments. According to committee testimony, the MVTF is responsible for covering three basic expenses: (1) emergency or need-based grants for veterans and their spouses and dependents; (2) the costs of administering the MVTF; and, since 1966, (3) a tuition grant program for the children of deceased, disabled, or missing-in-action veterans. Legislation has been introduced to transfer responsibility for directing investment of the fund from the State Administrative Board to the state treasurer *in statute* and to expand the options for investment of fund money.

THE CONTENT OF THE BILL:

Currently, Public Act 9 of 1946 charges the State Administrative Board with directing the investment, and authorizing (by resolution) all purchases, of the Michigan Veterans' Trust Fund. Investments are limited to bonds and various other government debt instruments, which must be purchased at current market price.

Senate Bill 797 would amend Public Act 9 of 1946 (MCL 35.605) to transfer the statutory authority to invest the MVTF to the state treasurer, to eliminate the current limitations on investments and purchasing requirements, and to give the treasurer the authority to invest the MVTF in the same manner as assets invested under the Public Employees Retirement System Investment Act. (Up to 70 percent of retirement fund assets may be invested in stocks, subject to certain restrictions.) The State Administrative Board would no longer be required to authorize MVTF purchases.

The bill would also require the state treasurer to report annually to the House and Senate Appropriations Committees on the revenues and expenditures of the MVTF. The report would have to specifically identify the interest and earnings of the MVTF, describe the impact of the expanded investment options on the amount of interest and earnings, and identify how the increased interest and earnings (if any) had been spent.

The bill is tie barred to Senate Joint Resolution (SJR) T, which would amend Article IX, Section 19 of the State Constitution to exempt certain funds, including the MVTF, from the prohibition on investment in stocks. (As passed by the Senate, SJR T would be submitted to voters at a special election held at the same time as the August 6, 2002 statewide primary election.)

Senate Bill 797 (1-9-02)

BACKGROUND INFORMATION:

Public Act 4 of 1943 created a post-war reserve fund of \$50 million “for the purpose of liquidating Michigan’s obligations, after the termination of the war, to its returning service men, their widows, or dependents”. Public Act 4 authorized the State Administrative Board to transfer immediately \$20 million from the general fund to the reserve fund, and directed the board and the state treasurer to transfer from the general fund to the reserve fund “accruing surplus revenues as promptly as accruing unappropriated revenues shall warrant, until the additional transfers shall bring the post-war reserve fund up to the total of \$50 million”. The post-war reserve fund was subsequently transferred to the Michigan Veterans’ Trust Fund when it was created by Public Act 9 of 1946. Public Act 9 specified that \$50 million of the transferred funds was to remain in the MVTF as a trust, and \$200,000 of the MVTF was to be transferred to an emergency loan fund to be used for veterans or their legal dependents “who may be engaged upon a course of instruction under any state or federal educational program”. According to the act, income accruing in the MVTF in excess of the \$50.2 million was to be used by the MVTF trustees to provide for the needs of Michigan veterans and their wives and dependents as well as to pay for the costs of administering the fund.

Acknowledging the need to protect the principal and earnings of the MVTF from being used for purposes other than to benefit veterans or their spouses or dependents, House Joint Resolution H (as approved by Ballot Proposal C in the 1996 General Election) established the MVTF in the state constitution and gave the state treasurer constitutional authority for the investment of the fund. The 1996 constitutional amendment also specified that all expenditures or transfers of trust fund assets, interest, or earnings other than the investment of the fund can be made only upon the authorization of a majority of the MVTF Board of Trustees. Such authorization must be based on a majority of the board’s vote that the expenditure or transfer is for the benefit of veterans or their spouses or dependents. Public Act 27 of 1995, which was tie-barred to HJR H, specified that the MVTF board of trustees, as established in the constitution, is responsible for administering the fund. This act also repealed the section of Public Act 9 of 1946 that both created the fund in statute and provided for the emergency loan fund, effective December 1997. The MVTF Board of Trustees reports that approximately \$21,000 is due to the fund in outstanding loans.

The MVTF trustees are also responsible for administering the tuition grant program established by Public Act 245 of 1935 and transferred to the MVTF trustees in 1966. Public Act 245 specifies that, subject to certain conditions, a child of a Michigan veteran who was killed or is missing in action or who was totally disabled or has died from a service-related injury or illness must be admitted to and may attend a state tax-supported educational or training institution of a secondary or college grade. Further, it allows such children to apply for and receive a \$2,800 grant per year for undergraduate education at *any* educational or training institution of a secondary or college grade that is located in the state—i.e., public or private. Public Act 245 states that “appropriations provided to the institutions or state board of education for this purpose shall be made to the Michigan veterans’ trust fund board of trustees”.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, Senate Bill 797 could increase future earnings of the Veterans’ Trust Fund (assuming Senate Joint Resolution T was approved by a vote of the people). Over the last three years, the MVTF had an annualized investment rate of return of 6.8 percent. From 1982 through 2001, the Michigan Public School Employees’ Retirement System (MPSERS) had an annualized rate of return of 12.2 percent. If this rate was realized in future years *and* the investment of the MVTF was directed in the same manner as the MPSERS, earnings from the fund’s \$50 million principal would increase by an average of \$2.7 million annually. Given the inherent nature of investments, however, past rates of return do not guarantee similar rates of return in the future. A more conservative estimate for investment return in future years would be the MSPERS actuarial assumption of 8 percent. Using this figure, annual earnings would increase by an average of \$600,000. Regardless of the actual rate of return, investment of the fund’s assets in the stock market would increase earnings risk and would result in larger differences in investment return from year to year, with the potential for negative earnings in any given year. (11-28-01)

ARGUMENTS:

For:

Currently, the principal of the Michigan Veterans Trust Fund is slightly above what it was when the

fund was created in 1946—\$50 million. Although \$50 million is no small change, the reality of inflation and other increased expenses mean that the annual earnings from the investment of the money do not go nearly as far as they did 55 years ago. Moreover, the fund is now used to pay for a tuition grant program that did not originally fall within its purview. Despite the increase in expenditures, it is still the case that fund money can only be invested in bonds and other government instruments. This effectively limits the MVTF to a “conservative strategy” of investment in “safe” but relatively low yield bonds and instruments. The bill would allow the fund’s assets to be invested in the same manner as state pension funds can be invested. The Public Employee Retirement System Investment Act allows up to 70 percent of retirement fund assets to be invested in domestic stocks, and also allows for investments in a broad array of other investments, including mortgages, real estate, international equities, and alternative investments. In fact, the legislature recently amended the act to increase the allowable investment in stocks, in recognition that this additional flexibility would allow pension managers to maximize investment returns to produce the greatest benefit for the state’s pension systems. Despite the potential for occasional, short-term losses, the expanded investment options will help increase the rate of return in the long term. The state treasurer would be a trustworthy steward of the money, who would be sensitive to the need to balance the interest in growth with the need for stability. Moreover, by capping the amount of money that could be invested in stocks, mortgages, etc., at 70 percent, the bill would provide additional assurance of the fund’s continued stability. It makes sense to acknowledge that the state treasurer has the responsibility for directing the investment of the MVTF *in statute* and to grant the treasurer expanded investment authority.

Response:

Although the bill would likely increase the fund’s earnings in the long run, it does not address what some veterans and their advocates believe should be the legislature’s “first priority”, namely the additional burden that the tuition grant program has placed upon the fund. Projections indicate that the total expenditure for the grants for the 2001 fiscal year was approximately \$930,000 and the total expenditure for the 2002 fiscal year grants will be approximately \$920,000. While the MVTF board of trustees acknowledges its responsibility for the tuition grant program, and the board and veterans generally support doing whatever they can to assist those who are eligible to receive such grants, some people have suggested that additional funding to

cover the grants would be welcome. Public Act 245 of 1935 provides for such an appropriation.

Against:

As the recent volatility of the stock market has demonstrated, the kinds of investments contemplated for MVTF assets by proponents of the bill may not produce the bountiful returns that are anticipated by the bill’s proponents; it is indeed possible that investments in stocks could produce a *negative* earnings amount in a given year. Is this wise, given that now the MVTF is entirely dependent on investment earnings for its program expenditures?

POSITIONS:

The Department of Military and Veterans’ Affairs supports the bill. (12-13-01)

The Commanders Group supports the bill. (12-13-01)

The American Legion, Department of Michigan supports the bill. (12-13-01)

The Veterans of Foreign Wars of the U.S., Department of Michigan supports the bill. (12-13-01)

Analyst: J. Caver

■ 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.