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INVEST STATE TRUST FUNDS IN STOCK MARKET

Senate Joint Resolution T (Substitute H-2)
Sponsor: Sen. Mat Dunaskiss

Senate Bill 796 (Substitute H-2)
Sponsor: Sen. George A. McManus Jr.

Senate Bill 798 (Substitute H-2)
Sponsor: Sen. Christopher D. Dingell

Senate Bill 799 (Substitute H-1)
Sponsor: Sen. Alma Wheeler Smith

Senate Bill 800 (Substitute H-1)
Sponsor: Sen. Loren Bennett

Senate Bill 801 (Substitute H-1)
Sponsor: Sen. Don Koivisto

First Analysis (2-20-02)

House Committee: Conservation and Outdoor Recreation
Senate Committee: Appropriations

THE APPARENT PROBLEM:

Ballot Proposal B, formerly House Joint Resolution M, was approved in the November, 1984, general election, and became Article IX, Section 35 of the state constitution, establishing the Natural Resources Trust Fund. The fund, established in statute by Public Act 101 of 1985, was a successor to the Kammer state recreational land acquisition trust of 1976, and to the trust established by the Heritage Trust Act of 1982, and its purpose is to provide a permanent source of money for land acquisition and for the development of public recreation facilities. Another aim of the fund was to protect the rights of Michigan Economic Development Authority (MEDA) bondholders, who purchased bonds in 1982 that were secured by money the economic development authority derived through the heritage trust.

The Natural Resources Trust Fund receives money from the oil, gas, and mineral royalties and lease fees from state-owned lands, other than those purchased with money from state or federal game or fish protection funds. The amount accumulated in the trust fund, after MEDA commitments are met, is currently capped at $400 million, exclusive of interest and earnings. Any excess is to be deposited as provided by law. Under Public Act 270 of 1984, effective March 29, 1985, the Michigan Strategic Fund replaced MEDA and acquired all its rights, responsibilities, and property. The $20 million annual commitments to MEDA were therefore paid into the Strategic Fund. MEDA commitments were paid until the debt service on MEDA's series 1982A bonds were paid off in 1994. The interest and earnings of the trust fund in each fiscal year are spent in the following fiscal year for the acquisition of land, the development of public recreational facilities, and the administration of the fund, which includes payment in lieu of taxes on state-owned land purchased through the fund. In addition, one-third of the money that has accrued to the trust fund's principal in a given fiscal year may be spent for those purposes in the following fiscal year, although this does not apply after the total money in the fund, exclusive of interest and earnings, equals the trust fund's ceiling. Of the amounts made available for expenditure from the trust fund in any fiscal year, at least 25 percent must be spent for land acquisition and not more than 25 percent must be spent for development of public recreational facilities. Grants to local governments or public authorities may be made, providing grants are used for permitted purposes and matched with local funds covering at least 25 percent of total project costs.

Ballot Proposal P, formerly Senate Joint Resolution E, was approved in the November, 1994, general election, an amendment to Article IX, Section 35 of the state constitution that ended the diversion of revenues from the trust fund to the Strategic Fund. The proposal was part of the package of legislation named the State Park Initiative, which redirected these revenues, instead, into a new state park endowment fund. It was intended that a permanent source of revenue be provided to support the improvement of the state's deteriorating parks system. (See *Background Information* for additional details.) The proposal specified that, until the trust fund reached its $400 million cap, up to 50 percent of the total oil and gas revenues received in one fiscal year, up to a total of $10 million each year, would be deposited into the proposed Genevieve Gillette State Park Endowment Fund. After the trust fund reached the $400 million cap, all oil and gas revenues, which would ordinarily have been deposited in the general fund, were, instead, to be deposited into the endowment fund until that fund reached an accumulated principal of $800 million fund. The Department of Natural Resources (DNR) estimated, at the time, that the state park endowment fund would reach its $800 million cap in 35 years. Money from that fund was to be spent to improve state parks, but only the interest and earnings from fund deposits could be spent.

Recently, a movement has been underway to spend more money now on the purchase of state land and the improvement of state parks, rather than saving it for the future. This is to be accomplished by allowing the funds to be invested more aggressively. Specifically, the proposal would allow the state treasurer, in investing the assets of the funds, to have the same authority as is granted to an investment fiduciary under the state-managed retirement funds. (Retirement funds may be invested in stocks and a variety of other investment vehicles, including mortgages, real estate, international equities, and so forth.) However, since the state constitution requires that the trust fund be invested conservatively, it is proposed that the question of amending the constitution be put before the voters at the next general election. The constitution also specifies that some of the annual oil and gas revenues may be spent while the trust fund builds to a $200 million ceiling. After that, only interest may be spent. Since rising revenues have increased the fund so that it has almost reached $200 million, the proposal would increase that ceiling to $500 million as well.

THE CONTENT OF THE BILLS AND THE JOINT RESOLUTION:

Senate Joint Resolution T proposes several amendments to Article IX of the state constitution, which generally prohibits state investment in stocks. The joint resolution would allow funds held as permanent funds or endowment funds, other than endowment funds created for charitable or educational purposes, to be invested as provided by law. Specifically, the joint resolution would provide that the Natural Resources Trust Fund, the State Parks Endowment Fund and the Veterans Trust Fund could be invested as provided by law.

In addition, the joint resolution would increase the cap on the accumulated principal of the Michigan Natural Resources Trust Fund, and would amend certain provisions pertaining to the Natural Resources Trust Fund and the State Parks Endowment Fund, and their allowable expenditures and the investment of their assets.

<u>Michigan Natural Resources Trust Fund.</u> The joint resolution would increase the limitation on the accumulated principal of the Natural Resources Trust Fund from $400 million to $500 million. In addition, the $200 million cap relating to grant fund appropriations would be increased to $500 million. Under current law, until the cap is reached, $10 million of the revenues from bonuses, rentals, delayed rentals, and royalties are deposited into the Michigan State Parks Endowment Fund. However, until the accumulated principal in the Natural Resources Trust Fund reaches the cap, not more than 50 percent of the total revenues from rentals, bonuses, and royalties is deposited into the State Parks Endowment Fund. When the trust fund reaches the cap, all revenue that would have been deposited into the fund is then deposited into the endowment fund.

<u>Michigan State Parks Endowment Fund.</u> Under current law, money in the endowment fund is expended for the operations, maintenance, and capital improvements at state parks. The joint resolution

would add that money in the endowment fund could also be expended for the acquisition of land or rights in land for state parks.

The endowment fund is capped at $800 million. Until the fund reaches the limit, the legislature cannot appropriate more than $5 million from the fund each fiscal year (that amount is adjusted annually for inflation). The joint resolution specifies that until the limit is reached, the legislature could appropriate not more than 50 percent of the money received through the Natural Resources Trust Fund in addition to interest, earnings, and any private contributions or other revenue to the fund.

Senate Bill 796 would amend the Natural Resources and Environmental Protection Act to increase the cap on the Michigan Natural Resources Trust fund from $400 million to $500 million. Until the cap is reached, $10 million of the revenues from the trust fund are deposited into the Michigan State Parks Endowment Fund. Further, the bill would increase the cap on grant fund appropriations from $200 million to $500 million.

The bill specifies that the state treasurer have the same authority to invest the assets of the trust fund as is granted to an investment fiduciary under the Public Employee Retirement System Investment Act.

In addition, the bill specifies that the Department of Natural Resources (DNR) would have to annually report on the revenues and expenditures of the trust fund, including the interest and earnings of the fund from the previous year, the investment performance of fund during the previous year, and the total amount of appropriations from the trust fund during the previous year. The report would be submitted to the Senate and House appropriations committees and the standing committees with jurisdiction over natural resources and the environment.

The bill also specifies that if property that was acquired with money from the trust fund is then sold or transferred by the state to a non-governmental agency, the state would then forward to the state treasurer for deposit into the trust fund an amount of money equal to the following:

- If the property was acquired with money only from the trust fund, the amount deposited into the trust fund would be the greatest amount of the net proceeds of the sale, the fair market value of the property at the time of the sale or transfer, or the amount of money that was expended from the fund to acquire the property.

- If the property was acquired with money from the trust fund and other funding sources governed by federal or state law, the amount of money deposited into the trust fund would be the product of an amount equal to the percentage of the funds contributed by the trust fund and the greatest amount listed above.

The bill would also specify that if within two years after a parcel of property that has been approved for acquisition or development by the legislature has not been acquired or remains undeveloped and is not open for public use, the Natural Resources Trust Fund Board would be required to report to the House and Senate standing committees with jurisdiction over natural resources and the environment on the status of the project and why it has not been completed.

The bill is tie-barred to Senate Joint Resolution T.

Senate Bill 798 would amend the Natural Resources and Environmental Protection Act to authorize the state treasurer to invest assets of the State Parks Endowment Fund in the same manner granted to an investment fiduciary pursuant to the Public Employee Retirement System Investment Act.

As under the provisions of Senate Joint Resolution T, money from the endowment fund could be expended for the acquisition of land or rights in land for state parks. In addition, until the endowment fund reaches the $800 million cap, the legislature could not appropriate more than 50 percent of the money received from the Natural Resources Trust fund (rather than $5 million, adjusted for inflation), plus interest, earnings, and any private or contributions or other revenue to the fund. The bill would also require the DNR to submit a report to the Senate and House on the revenues and expenditures of the trust fund, including the interest and earnings of the fund from the previous year, the investment performance of fund during the previous year, and the total amount of appropriations from the trust fund during the previous year. The report would be submitted to the Senate and House appropriations committees and the standing committees with jurisdiction over natural resources and the environment.

The bill is tie-barred to Senate Joint Resolution T.

Senate Bills 799 and 800 would amend the Natural Resources and Environmental Protection Act to authorize the state treasurer to invest assets from certain trust funds in the same manner as is granted to an investment fiduciary under the Public Employee Retirement System Investment Act. Senate Bill 799 would authorize the investment of assets from the Nongame Fish and Wildlife Trust Fund. Senate Bill 800 would authorize the investment of assets from the Game and Fish Protection Trust Fund.

Senate Bill 801 would amend the Michigan Civilian Conservation Corps Act to authorize the state treasurer to invest assets from the Michigan Civilian Conservation Corps Endowment Fund in the same manner that is granted to an investment fiduciary under the Public Employee Retirement System Investment Act.

In addition, the Senate Bills 799-801 would require the DNR to report to the House and Senate appropriations committees and the standing committees with jurisdiction over natural resources and the environment on the interest and earnings, the investment performance, and the total amount of appropriations from each of the funds.

Senate Bills 799-801 are each tie-barred to Senate Joint Resolution T.

BACKGROUND INFORMATION:

Michigan's state park and recreation area system, operated by the Department of Natural Resources (DNR), incorporates 120 miles of Great Lakes frontage; over 260,000 acres of recreational land; 11,000 miles of scenic inland lakes and rivers; sand dunes; waterfalls; wetlands; and historical sites such as museums, forts, logging camps, sawmills, and farms. From its conception in 1919, the state park system grew to be the "crown jewel" of the state's natural resources, and now consists of almost 100 sites that contain over 14,000 campsites. The state's pride in its parks, however, has not always translated into a corresponding commitment to provide sufficient funds for their upkeep. In 1994, it was noted that park user fees -- first implemented in 1950 -- had increased to the point that users mainly funded the park system. Such a system failed to provide adequate funding for even the most basic services. Thousands of vacationing citizens were affected: continuous increases in user fees threatened to exclude some citizens from the parks; and poor maintenance had persuaded others to switch to private campgrounds.

The legislature and the DNR responded to this situation in 1994 with a plan that evolved around the concept of a state park endowment fund, from which interest and earnings were to be drawn to supplement current appropriations. It was hoped that this would provide the parks with a continuous, stable source of revenue. The plan, named the State Park Initiative, included Public Act 79 of 1994, which established the Genevieve Gillette State Parks Endowment Fund; Public Act 78 of 1994, which provided immunity from liability to volunteers working in state parks; Public Act 102 of 1994, which amended the Michigan Tourism Policy Act to add recognition of state and locally managed recreational opportunities as one of the tourism policy act's goals; Public Act 119 of 1994, which made fund transfers to state parks possible by permitting taxpayers to use a state income tax checkoff to buy annual state park passes; and Public Act 120 of 1994, which specified that general fund appropriations to the parks system must be adjusted annually for inflation. In conjunction with the state park initiative, Public Act 107 of 1994 appropriated $40 million from the sale of the state accident fund to the proposed state parks endowment fund, and Public Act 108 of 1994 permitted $20 million of the proceeds of the accident fund's sale to be appropriated for a proposed Civilian Conservation Corps Endowment Fund. As part of this plan, the voters approved Ballot Proposal P, which further supplemented the state parks' budget by ending the diversion of revenues from the Michigan Natural Resources Trust Fund and redirecting a portion of the revenues into the state park endowment fund.

FISCAL IMPLICATIONS:

With regard to SJR T and Senate Bill 796, the House Fiscal Agency (HFA) notes that the increase in the cap on the accumulated principal of the Natural Resources Trust Fund would delay the deposit to the State Park Endowment Fund of all revenue from royalties on state-owned minerals. The resolution would also increase the allowable spending level from the trust fund. The HFA calculates that approximately $14 million would have been available for expenditure if the $200 million cap on grant fund appropriations had been reached. If the cap is increased to $500 million, this amount would be approximately $27 million.

Under the resolution, the state treasurer would be permitted to invest trust fund assets in the same manner as state managed retirement funds. The HFA estimates that the marginal increase in return to the trust fund would be 4 percent. The assumed rate of return for state managed retirement funds is 8 percent. However, regardless of the actual rate of return, investment in the stock market would increase earnings risk and result in larger differences in investment return from year to year. The potential exists for negative earnings in any given year.

According to the HFA, if the resolution is not approved, grant funds to local governments would be reduced by 50 percent to approximately $14 million annually.

With regard to Senate Bill 798, the HFA reports that the amount available for annual appropriation to state parks would increase; the executive recommendation for fiscal year 2002-2003 is $5,248,500. (2-15-02)

ARGUMENTS:

For:

The joint resolution and the bills are part of a ballot campaign that would amend the state constitution in order to free more money for the purchase of state land and state parks improvement. Under the legislation, money in the Michigan Natural Resources Trust Fund (MNRTF) and the State Parks Endowment Fund would continue to grow, but more money would be made available for conservation and outdoor recreational projects. The bills propose giving the state treasurer the flexibility to invest a myriad of funds and endowments in the same manner as state pension funds are currently invested. This could yield millions of dollars in additional interest income.

The bills also propose increasing the maximum amount of money that may be withdrawn and expended annually from the trust fund and the endowment fund. The endowment fund receives transfers of $10 million per year from the MRTF for state parks operations, maintenance, and capital improvements. Each state fiscal year the legislature may appropriate up to $5 million of the fund, annually adjusted for inflation, until the endowment fund reaches an accumulated principal of $800 million. Under the bills, the appropriation would be increased to $10 million annually. The endowment fund was established under a provision of Ballot Proposal P in 1994, generally referred to as the State Park Initiative.

Since it was established in 1976, the MNRTF has been a critically important tool for conservation in Michigan, and has been the main source of funding for conservation and outdoor recreation projects. Revenue for the fund is derived from the sale of oil, gas, and mineral leases and royalties from oil, gas, and mineral extraction on state-owned land. Under Article IX, Section 35 of the state constitution, the interest and earnings of the trust fund may only be spent to acquire land for recreational uses, to protect the land because of its environmental importance or scenic beauty, or to develop public recreational facilities. (Among the fund's most recent benefits was a grant to acquire more than 6,000 acres of conservation land at the tip of the Keweenaw Peninsula.)

Against:

Under Ballot Proposal P of 1994, the voters approved transferring $10 million per from the Michigan Natural Resources Trust Fund (MNRTF) year to the State Park Endowment Fund for state parks operations, maintenance, and capital improvements. The ballot proposal specified, in part, that, until the endowment fund reaches an accumulated principal of $800 million, each state fiscal year the legislature may appropriate up to $5 million of the fund, annually adjusted for inflation. However, under the bills, this appropriation would be increased to $10 million per year. Such spending would ultimately delay the endowment fund's growth. Moreover, the restriction of $5 million annually was specified, when the ballot proposal was first proposed, in order to build the endowment fund as fast as possible. This provision was approved by the voters and should not be changed now.

Against:

The provisions of the bills that would allow the assets of the trust fund and the endowment fund to be invested aggressively focuses only on the gains that might be made in a bull market. However, there is another side to this coin: as noted by the House Fiscal Agency in its analyses of the bills, "investment in the stock market would increase earnings risk and result in larger differences in investment return from year to year. The potential exists for negative earnings in any given year."

POSITIONS:

The Department of Natural Resources (DNR) supports the bills. (2-19-02)

The Michigan Environmental Council (MEC) supports the bills. (2-19-02)

The Nature Conservancy supports the bills. (2-19-02)

The Michigan Oil and Gas Association (MOGA) supports the bills. (2-19-02)

The Michigan United Conservation Clubs (MUCC) supports the bills. (2-19-02)

The Michigan Municipal league (MML) supports the bills. (2-14-02)

The Michigan Chamber of Commerce supports the bills. (2-14-02)

The Michigan Recreation and Park Association supports the bills. (2-14-02)

Analyst: R. Young

■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.