Legislative Analysis

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PUBLIC EMPLOYEE RETIREMENT SYSTEMS: AUTHORIZED INVESTMENTS

House Bill 6500
Sponsor: Rep. Robert Jones
Committee: Senior Health, Security and Retirement

Complete to 11-10-08

A SUMMARY OF HOUSE BILL 6500 AS INTRODUCED 9-24-08

House Bill 6500 would amend the Public Employee Retirement System Act to address how assets can be invested.

The Public Employee Retirement System Investment Act authorizes the investment of assets of public employee retirement systems in Michigan, and places limitations on the ways in which those funds can be invested. The act applies to all retirement systems operated by the state or by local units of government. It has been amended periodically to bring it up to date with current investment practices. The purpose of these periodic amendments has been to balance the dual aims of ensuring prudence in investment decisions to safeguard public assets and allowing pension managers flexibility to maximize investment returns. The act was updated in 1982, 1996, and again in 2000.

The bill would make the following changes.

Real Estate Investment Trusts.
Current law allows investment of up to 5 percent of a system's assets in publicly or privately issued real estate investment trusts (REIT) or certain other real or personal property as prescribed under the act. The bill would increase the maximum investment to 10 percent.

Currently, in addition to the limit cited above, an investment fiduciary of a system with assets of more than $100 million can form one or more limited partnerships, limited liability companies, trusts, or other entities to hold title to, improve, lease, manage, develop, maintain, or operate real or personal property. The liability of the investor cannot exceed the amount of an investment under federal law or the laws of any U.S. state, district, or territory. The bill would amend this provision to allow such a fiduciary to form or invest in such entities, and also to limit investor liability based on laws of foreign countries, in addition to U.S. law. The limit on these kinds of investments currently cannot exceed 5 percent of assets; the bill would increase that to 10 percent.

Currently, if the investment fiduciary of a system is the State Treasurer then the investments described in the above paragraphs can exceed 5 percent of the assets of the system. The bill would allow investments by the State Treasurer to exceed the new limits of 10 percent of the assets of the system.

Private Equity.

Under the bill, an investment fiduciary of a system having assets of less than $250 million could invest up to 5 percent of its assets in private equity. However, if the system has assets of less than $250 million, the investments would have to be made through a "fund of funds" vehicle.

An investment fiduciary of a system with $250 million or more in assets could invest up to 10 percent of its assets in private equity. A system having assets of $1 billion or more could invest up to 15 percent of its assets in private equity. If the investment fiduciary is the State Treasurer, investments described in this section would not be subject to a percentage of the total assets limitation.

"Private Equity" would be defined to mean an asset class consisting of equity or debt securities in entities that are not publicly traded, which could include investments in leveraged buyouts, venture capital, growth capital, distressed or special situations, mezzanine capital, and secondary investments in equity or debt interests. The bill would define "fund of funds" to mean an investment fund that uses an investment strategy of holding a portfolio of other investment funds rather than investing directly in shares, bonds, or other securities.

Other Investments

The act allows investment fiduciaries to invest in "investments not otherwise qualified" under the act, subject to certain limits. These limits would not be altered except that the bill would say that the State Treasurer could invest not more than 25 percent (rather than not more than 20 percent) of a system's assets in these investments.

Derivatives

Under current law an investment fiduciary can invest in various derivatives to enhance portfolio performances. The aggregate market value of the underlying security, future, or other instrument or index made under this section cannot not exceed 15 percent of the assets of the system (although some kinds of investment are outside of the limit). Under the bill, the aggregate market value could not exceed 30 percent of the assets of the system.

Foreign Securities

The act limits the amount of investments in foreign securities to 20 percent of a system's assets. The bill would specify that the State Treasurer could invest more than 20 percent of a system's assets in foreign securities.

Costs of Training and Education

The act currently allows an investment fiduciary to use a portion of the income of the system to defray costs of investing, managing, and protecting the assets of the system. The bill would also allow for defraying the costs of providing professional training and education.

Repealer

The bill would repeal a section that establishes a set of principles (the MacBride Principles) for investing in companies that do business in Northern Ireland.

FISCAL IMPACT:

The bill's fiscal impact is indeterminate.

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