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BILL ANALYSIS

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Senate Bill 1129 (as enacted) **PUBLIC ACT 329 of 2012**
Sponsor: Senator Patrick J. Colbeck
Senate Committee: Appropriations
House Committee: Appropriations

Date Completed: 10-15-12

CONTENT

The bill amended the Revised Municipal Finance Act to allow a municipality (county, city village, or township) to issue a municipal security to pay all or part of the costs of the unfunded pension liability for a retirement program or the costs of the unfunded accrued health care liability, under certain circumstances.

Specifically, the bill added Section 518 to allow a municipality to issue a municipal security, through December 31, 2014, to pay all or part of the costs of the unfunded pension liability for a retirement program, in connection with the partial or complete cessation of accruals to a defined benefit (DB) plan or the closure of the DB plan to new or existing employees and the implementation of a defined contribution (DC) plan, or to fund costs of a municipality that has already ceased accruals to a DB plan. A municipality may issue such a security by ordinance or resolution of its governing body and without a vote of its electors. The amount of taxes necessary to pay the principal and interest on that municipal security, together with the taxes levied for the same year, may not exceed the limit authorized by law.

Also, through December 31, 2014, a municipality may issue a municipal security, by ordinance or resolution of its governing body and without a vote of its electors, to pay the costs of the unfunded accrued health care liability provided the amount of taxes necessary to pay the principal and interest on that municipal security, together with the taxes levied for the same year, does not exceed the limit authorized by law, or to refund all or a portion of a contract obligation issued for the same purpose. Postemployment health care or benefits may be funded by the municipality; this funding will not constitute a contract to pay the postemployment health care benefits.

Before issuing a municipal security for these purposes, the municipality must publish a notice of intent to issue the security that meets the requirements of a notice of intent for other municipal securities, as outlined in Section 517(2) of the Act. The municipality also must prepare and make available to the public a comprehensive financial plan that includes all of the following:

-- An analysis of the current and future obligations with respect to each retirement program and each postemployment health care benefit program of the municipality.
-- Evidence that the issuance of the municipal security together with other funds lawfully available will be sufficient to eliminate the unfunded pension liability or the unfunded accrued health care liability.
-- A debt service amortization schedule and a description of actions required to satisfy the schedule.
-- A certification by the person preparing the plan that the comprehensive financial plan is complete and accurate.

In addition, if the proceeds of the borrowing are to be deposited in a health care trust fund, there must be a plan in place from the municipality to mitigate the increase in health care costs. The plan may include a wellness program that promotes the maintenance or improvement of healthy behaviors.

The bill exempts such municipal securities and the interest and income from them, from taxation by the State or a political subdivision of the State. A municipality issuing these securities may enter into indentures or other agreements with trustees and escrow agents for the issuance, administration, or payment of the securities.

The proceeds of a municipal security issued under Section 518 may be used to pay the costs of issuance. Except for a refunding, the proceeds of a municipal security to cover unfunded health care liability must be deposited in a health care trust fund, a trust fund created by the issuer that has as its beneficiary a health care trust fund, or, for a municipality, a restricted fund within a trust that would only be used to retire municipal securities. A municipality must have the power to create such a trust and the trust must invest its funds in the same manner as funds invested by a health care trust fund. The trust must be tax-exempt under the Internal Revenue Code and report its financial conditions according to generally accepted accounting principles.

A municipality must obtain the approval of the Department of Treasury before issuing a municipal security under Section 518.

The bill prohibits a municipality that has issued such a security from changing the benefit structure of the DB plan if that plan is undergoing the partial cessation of accruals. A municipality may, however, reduce benefits of that plan for years of services accruing after the issuance of the security.

The bill also prohibits a municipality from issuing a security under Section 518 unless it has a credit rating within the category of AA or higher, or the equivalent, by at least one nationally accredited rating agency. A municipality that issues a municipal security to pay for all or part of the costs of its unfunded pension liability must covenant with the security holders and the State that it will not, after the municipal security is issued and outstanding, rescind whatever action it has taken to make a partial or complete cessation of accruals to a DB plan or the closure of the DB plan for new or existing employees.

The Act requires a municipal security to meet one or more of the following conditions, as determined by the Department of Treasury, in order to be sold at a discount exceeding 10% of the principal amount:

-- The sale will result in the more even distribution for the municipality of total debt service on proposed and outstanding municipal securities.
-- The sale will result in an interest cost saving when compared to the best available alternative that does not include a municipal security being sold at a discount exceeding 10% of the principal amount.
-- The issuance is based on the availability of specific revenue previously pledged for another purpose and lawfully available for this purpose.
-- The security is issued to this State or the Federal government to secure a loan or agreement.

Under the bill, the municipal security also must be issued pursuant to Section 518.

The Act allows municipal securities of a single issue to mature serially or be subject to mandatory redemptions, or both, with maturities as fixed by the municipality's governing body. In any case, the first maturity or mandatory redemption date cannot occur later than five years after the date of issuance, and the total principal amount maturing or subject to mandatory redemption after four years from the date of issuance cannot be less than one-fifth of the total principal amount maturing or subject to mandatory redemption in any subsequent year.

The bill exempts municipal securities issued under Section 518 from these maturity and mandatory redemption requirements.

The bill defines the following terms:

-- "Defined contribution plan" means a retirement program that provides for an individual account for each participant and for benefits based solely upon the amount contributed to his or her account, and any income, expenses,

-- gains, and losses credited or charged to the account, and any forfeitures and accounts of other participants that may be allocated to his or her account.
-- "Defined benefit plan" means a retirement program other than a defined contribution plan.
-- "Retirement program" means a program of rights and obligations that a municipality establishes, maintains, or participates in and that, by its express terms or as a result of surrounding circumstances, either provides retirement income to participants, or results in a deferral of income for periods extending to the termination of covered employment or beyond, or both.
-- "Unfunded accrued health care liability" means the difference between assets and liabilities of a health care trust fund as determined by an actuarial study according to the most recent governmental accounting standards board's applicable standards.
-- "Unfunded pension liability" means the amount a defined benefit plan's liabilities exceed its assets according to the most recent governmental accounting standards board's applicable standards.

The bill also defines "health care trust fund" as a trust or fund used exclusively to provide funding for postemployment health care benefits for public employee retirees of a municipality. It also includes the retiree health fund vehicle administered by the Municipal Employees Retirement System for a municipality that has adopted such a system to provide funding for postemployment health care benefits for public employee retirees.

The bill took effect on October 9, 2012.

MCL 141.2103 et al.

Legislative Analyst: Cameron S. Mock

FISCAL IMPACT

State: The Department of Treasury will see increased administrative costs associated with this bill, due to the requirement of reviewing any securities proposed to be issued for the purpose of paying off the unfunded accrued liabilities of a municipality's retiree health care or closed defined benefit pension system.

Local: The fiscal impact on local municipalities is indeterminate. Allowing municipalities to issue securities through December 31, 2014, to finance the unfunded accrued liabilities associated with a closed defined benefit pension plan or a retiree health care plan will provide an additional financial instrument with which to pay down the unfunded accrued liability (UAL). However, the actual resulting fiscal impact is unknown and will depend upon the cost of the security compared to market performance, the impact (if any) on the municipality's credit rating, and the potential risks associated with converting a "soft" debt of the municipality (the pension or health UAL) into a "hard" debt with a rigid and fixed repayment schedule.

Fiscal Analyst: Kathryn Summers