Legislative Analysis

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DETROIT BANKRUPTCY-RELATED PACKAGE

House Bill 5566
Sponsor: Rep. John Walsh

House Bill 5567
Sponsor: Rep. John Kivela

House Bill 5568
Sponsor: Rep. Gail Haines

House Bill 5569
Sponsor: Rep. Andrea LaFontaine

House Bill 5570
Sponsor: Rep. Ken Yonker

House Bill 5571
Sponsor: Rep. Ken Goike

House Bill 5572
Sponsor: Rep. John Olumba

House Bill 5573
Sponsor: Rep. Alberta Tinsley Talabi

House Bill 5574
Sponsor: Rep. Thomas F. Stallworth III

House Bill 5575
Sponsor: Rep. Fred Durhal, Jr.

Committee: Detroit's Recovery and Michigan's Future
Complete to 5-12-14

A SUMMARY OF HOUSE BILLS 5566-5575 AS INTRODUCED 5-8-14

<u>Brief Summary:</u>

Generally speaking, this package of bills would do the following:

- Authorize the distribution of $194.8 million from the state's Budget Stabilization Fund to the retirement systems of the City of Detroit for Fiscal Year 2013-14. The money would first be transferred and appropriated to a newly-created fund administered by a Settlement Administration Authority, and then could be paid to the retirement systems if certain conditions are met. (HB 5572, HB 5574 and HB 5575)

- Require an annual deposit into the BSF of $17.5 million from tobacco settlement revenue from Fiscal Year 2015 through Fiscal Year 2035. (HB 5573)

- Create a 7-member Oversight Commission, to include the governor and the mayor, which, among other things, <u>would</u>: ensure that a "qualified city" (i.e., Detroit) is meeting certain statutory requirements; review and approve the city's four-year financial plan; establish and maintain programs and requirements for the responsible fiscal management of the city; review and approve all applicable contracts, including all contracts for goods and services exceeding $750,000 or that exceed two years; approve or reject all collective bargaining agreements to which the city is a party after approval by the governing body and mayor; and approve or reject decisions of arbitration panels under Public Act 312 of 1969, dealing with compulsory arbitration of police and fire labor disputes. Also the commission could: review and approve proposed and amended operational budgets of the city, which could not take effect unless approved by the commission; approve the appointment of a qualified city's chief financial officer; review and approve requests by the city to issue debt; require the city to solicit competitive bids; review compliance with deficit reduction plans; and review and approve or revise the city's consensus revenue estimate. (HB 5566 would create a new act establishing this commission and is described in more detail later.)

- Allow the commission to grant the city waivers from oversight if certain specified conditions are met and allow the commission to dissolve itself under specified circumstances (as detailed later in the description of HB 5566).

- Require the city to establish the position of chief financial officer; to adopt a four-year financial plan; and to hold revenue estimating conferences each September and February. The financial officer would be appointed by the mayor subject to the approval of the governing body of the city and, if applicable, the Oversight Commission. (HB 5567)

- Specify that new employees of the City of Detroit as of January 1, 2015, could not participate in a defined benefit plan but could only participate in a defined contribution (401k-style) system, if there was one, and could not receive any retirement health care insurance benefit. (Neither of these provisions would apply if they were contrary to a collective bargaining agreement in effect on January 1, 2015.) In lieu of any retirement health care benefit, the city could make a matching contribution up to 2% of base pay to an appropriate tax-deferred retirement account. The city also could contribute up to 4% of base pay to an appropriate tax-deferred retirement account and could match employer contributions up to an additional 3% of base pay. [These benefit levels are comparable to those now provided to most newly hired state employees.] (HB 5568)

- Restrict the calculation, as of January 1, 2015, of a pension benefit under a defined benefit plan to include only base pay; this would not apply to years of service accrued prior to that date. The term "base pay" excludes overtime, accumulated sick leave, bonuses, accrued vacation pay, one-time lump sum payments, and the cost of fringe benefits. This would not apply if contrary to a collective bargaining agreement in effect on January 1, 2015. (HB 5568)

- Prohibit the annual pension benefit from including an additional payment based on the rate of investment return earned on the retirement system's assets, as of January 1, 2015. This would not apply if contrary to a collective bargaining agreement in effect on January 1, 2015. (HB 5568)

- Limit what the City of Detroit pays toward employee medical benefit plans to the amounts specified in the Publicly Funded Health Insurance Contribution Act; that act limits public employer contributions to either a dollar amount ("hard cap") per employee or, alternatively, to no more than 80 percent of the total annual costs of all the medical benefit plans it offers or contributes to for its employees. Under that act, a local unit of government can exempt itself from the contribution limit in any year with a two-thirds vote of the governing body and approval by the mayor; this exemption option would no longer apply to the City of Detroit. (HB 5569)

- Prevent the property tax millage that voters in each of three counties have approved to support the Detroit Institute of Art from being renewed. The millage would be limited to its current 10 years in duration (rather than the permitted 20 years), and a new tax would not be permitted. (HB 5571)

- Require Detroit's public employee retirement system to establish an investment committee, which would select the system's chief financial officer and its advisors and consultants; restrict out-of-state travel of those affiliated with the system; and require reporting of out-of-state travel expenditures. (HB 5570)

- Define a "qualified city" as a city with a population of more than 600,000 for which a plan for adjustment was approved and entered by a United States bankruptcy court. A "plan for adjustment" refers to the plan for adjustment of debts of a qualified city. (These definitions are in House Bill 5566, and similar terms apply throughout the proposed legislation.)

FISCAL IMPACT:

The bills would create a cost to the state by appropriating $194.8 million out of the state's BSF in FY 2013-14 to be utilized for Detroit's retirement systems (via HBs 5574 and 5575). The BSF is currently projected to have a balance of $588.7 million at the close of FY 2013-14. The bills would reduce that balance to approximately $393.9 million.

The appropriation amount of $194.8 million reportedly represents a discounted lump sum payment equivalent to the state making an annual payment of $17.5 million to the pension systems for 20 years. HB 5573 would provide for $17.5 million in annual tobacco settlement revenues received by the state to be deposited into the BSF from FY 2014-15 through FY 2034-35. That time period covers 21 years, so $367.5 million would eventually be repaid to the BSF under the bill's provisions. (These transactions effectively represent the state borrowing funds from itself, avoiding interest and other borrowing costs that would be involved if the funds were borrowed from an outsider lender.) The FY 2014-15 Executive Recommendation reserved (that is, did not appropriate) $17.5 million in available tobacco settlement revenues for this purpose.

HB 5566 would appropriate $900,000 in GF/GP revenue to the Department of Treasury for the Oversight Commission created by that bill. An indeterminate amount of ongoing costs would be incurred by the state as state officials monitor the city's financial condition as part of the Oversight Commission and Settlement Administration Authority created by the bills.

HB 5572 would have no direct fiscal impact but could have future fiscal implications by allowing appropriations out of the BSF for any purpose provided by law. Currently, the Management and Budget Act must be amended in order to appropriate funds out of the BSF for purposes not specifically provided for in the act.

The bills would have a significant fiscal impact on the City of Detroit, in the context of the city's bankruptcy proceedings and the proposed settlement between the city, the state, and private organizations related to those proceedings. A full analysis of the proceedings exceeds the scope of this analysis. The payment of $194.8 million to the city's retirement systems would reduce the liabilities of those systems.

Generally, HBs 5567, 5568, 5569, and 5570 would reduce or limit expenditures by the city. The fiscal impact of moving new employees from a defined benefit retirement plan to a defined contribution retirement plan would depend on the precise provisions and associated normal costs of those plans. Generally, closing a defined benefit retirement plan creates accelerated funding requirements for unfunded actuarial accrued liability costs to maintain actuarial soundness.

HB 5571 would have a potential fiscal impact on the Detroit Institute of Arts by prohibiting the renewal of the existing 10-year voter-approved 0.2 millage for the institute in the counties of Macomb, Oakland, and Wayne. This millage currently generates about $23 million in revenue per year.

The Bills in Brief:

The following bills are part of this proposed legislation.

House Bill 5566 would create the Oversight Commission Act. It also appropriates $900,000 from the General Fund to the Department of Treasury for commission resources; and contains a list of legislative findings and declarations as justification for the act.

House Bill 5567 would amend the Home Rule City Act to require the city to establish the position of chief financial officer; to adopt a four-year financial plan; and to hold revenue estimating conferences each September and February.

House Bill 5568 would amend the Home Rule City Act to require a defined contribution system for new employees; restrict the calculation of pension benefits under an existing defined benefit system to base pay for future years of service; and prohibit the annual pension benefit from including an additional payment based on the rate of investment return earned on the retirement system's assets.

House Bill 5569 would amend the Publicly Funded Health Insurance Contribution Act to eliminate the city's ability to opt out under that act from limits on the amounts the city is allowed to pay toward employee medical benefit plans.

House Bill 5570 would amend the Public Employee Retirement System Investment Act to require the city's retirement system to establish an investment committee, which would select, monitor, and evaluate the system's chief financial officer and its advisors and consultants; to restrict out-of-state travel of those affiliated with the system; and to require reporting of out-of-state travel expenditures.

House Bill 5571 would amend the Art Institute Authorities Act to prohibit the renewal of the existing voter-approved 10-year millage and prohibit voter approval of a new millage.

House Bill 5572 would amend the Management and Budget Act to permit the legislature to make an appropriation out of the Budget Stabilization Fund for any purpose it provides by law.

House Bill 5573 would amend the Michigan Trust Fund Act to require an annual deposit into the BSF of $17.5 million from tobacco settlement revenue from Fiscal Year 2015 through Fiscal Year 2035.

House Bill 5574 would amend the Management and Budget Act to transfer and appropriate $194.8 million from the BSF to the Settlement Administration Fund.

House Bill 5575 would create the Michigan Settlement Administration Authority Act, under which the authority could disburse the $194.8 million in the fund to the police and fire retirement system and the general retirement system of the City of Detroit for the benefit of qualified beneficiaries if both (1) the bankruptcy court has entered an order approving a plan of adjustment of debts for the city; and (2) the terms and conditions of the contribution agreement (within the plan of agreement) have been satisfied.

The authority would have a five-member board chaired by the state treasurer. The other members would be the director of the Department of Licensing and Regulatory Affairs; one member appointed by the governor with the advice and consent of the Senate who has knowledge, skill, or experience in the legal field of bankruptcy; one appointed by the governor from a list of two or more nominated by the Speaker of the House; and one appointed from a list of two or more nominated by the Senate Majority Leader. The nominees in each case would need knowledge, skill, or experience in bankruptcy, finance, accounting, or another relevant field.

The bill contains a list of findings and declarations that describe the connection of the provisions to Detroit's bankruptcy case and city pension benefits, and how they will be beneficial to the entire state.

One additional bill is yet to be introduced; it is expected to amend Public Act 312 of 1969, dealing with compulsory arbitration of police and fire labor disputes.

Summary of House Bill 5566:

The bill creates the Oversight Commission Act. Under the new act, a seven-member commission would provide wide-ranging oversight for the City of Detroit beginning on the effective date of the "plan for adjustment" or the effective date of the new act, whichever is later. "Plan for adjustment" refers to the plan for the adjustment of debts approved and entered by a United States bankruptcy court. The seven members include:

- The governor (or a designee)
- The state treasurer
- The director of the Department of Technology, Management and Budget (or a designee)
- One member appointed by the governor who is a resident of the city and who has knowledge, skill, or experience in business or finance
- The mayor (chief executive officer) of the city (or a designee)
- One member appointed by the governor from a list of three or more individuals nominated by the Senate Majority Leader; one of the nominees would need to be a city resident and all would need knowledge, skill, or experience in business or finance.
- One member appointed by the governor from a list of three or more individuals nominated by the Speaker of the House of Representatives; one of the nominees would need to be a city resident and all would need knowledge, skill, or experience in business or finance.

The commission would have to meet at least monthly, and meetings would have to be conducted in compliance with the Open Meetings Act, although the bylaws could permit attendance by telecommunication or other electronic equipment; and writings of the commission would be subject to the Freedom of Information Act.

Most of the duties and powers of the commission are described in the first paragraph (bullet point) of this summary. Generally, the commission would have to establish and maintain programs and requirements for the responsible fiscal management of the city, including: increased managerial accountability; the streamlining of city services; improved tax collection; revisions to procurement practices, including competitive bidding procedures; and the review of compensation and benefits of city employees and recommendations for adjustments where necessary. The commission would also be charged with ensuring that the city comply with provisions in the Revised Municipal Finance Act and the Uniform Budget and Accounting Act, as well as with the various amendments to state statute made by the other bills in the package of legislation.

The city would have to present written reports to the commission when so required regarding its financial stability and would have to allow the commission to audit or inspect financial statements, actuarial reports, revenue estimates, and any and all other documents, data, reports, or findings the commission considers necessary to carry out its purposes.

The commission could require the city's chief financial officer to provide the commission with information it requested related to the city's finances, and could require the officer to attend commission meetings. If the financial officer failed to comply, the commission could require the city to remove the financial officer.

The commission would have to file, on June 1 and December 1, of each year a written report with the governor, with a copy to the House Speaker and Senate Majority Leader.

The commission could grant the city a waiver from one or more of the requirements if all of the following conditions are met:

- The commission certified that the city had adopted and adhered to deficit-free budgets for three consecutive years;

- The state treasurer and the city's chief financial officer certify that all municipal securities or debt obligations during the immediately preceding fiscal year and current fiscal year satisfied the capital and other financial reporting requirements of the city during that period and there is substantial likelihood that municipal securities and debt obligations can be sold in the general public market during the remainder of the current fiscal year and the immediately succeeding fiscal year in amounts sufficient to substantially satisfy all the capital and other financial requirements of the city during those periods in accordance with the city's financial plan;

- The city's financial plan projects a balanced budget for the current and succeeding three fiscal years;

- The city has been assigned a credit rating with the category A- or higher, or the equivalent, by at least one nationally recognized rating agency or has otherwise demonstrated to the commission's satisfaction that the city has sufficient ability to borrow in the municipal securities market;

- The city did not violate the plan for adjustment in the immediately preceding fiscal year and is not in violation in the current fiscal year;

- The state treasurer certifies that the city is in compliance with the Uniform Budgeting and Accounting Act; and

- The commission certifies that the city is in substantial compliance with the Oversight Commission Act.

A waiver would be rescinded if any of the following, where applicable, have occurred or are likely to occur, and the waiver could be rescinded if the circumstances no longer exist:

- The city fails to pay principal of or interest on any municipal securities when due or payable;

- The city incurs a budget deficit in a fiscal year equal to or more than 5% of the total expenditures in that year;

- The city issues municipal securities without the authorization of the commission or in violation of the Revised Municipal Finance Act;

- The city violates the Oversight Commission Act or any mandatory financial controls in a manner that substantially impairs its ability to pay principal of or interest on municipal securities when due and payable or its ability to adhere to a balanced budget;

- The city violates any provisions of the plan for adjustment;

- The state treasurer and the city's chief financial officer fail to certify that municipal security and debt requirements cited earlier have been met; or

- If the city's chief financial officer has resigned, been terminated, or been removed, or the office has otherwise become vacant and a successor has not been appointed with 180 days of the vacancy.

The commission could dissolve itself if it has waived one or more requirements each year for the previous ten consecutive fiscal years and the plan for adjustment has expired.

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