Legislative Analysis

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DETROIT BANKRUPTCY-RELATED PACKAGE

House Bill 5566 (Substitute H-3)
Sponsor: Rep. John Walsh

House Bill 5567 (Substitute H-2)
Sponsor: Rep. John Kivela

House Bill 5568 (Substitute H-2)
Sponsor: Rep. Gail Haines

House Bill 5569 as introduced
Sponsor: Rep. Andrea LaFontaine

House Bill 5570 (Substitute H-3)
Sponsor: Rep. Ken Yonker

House Bill 5571 (Substitute H-1)
Sponsor: Rep. Ken Goike

House Bill 5572 as introduced
Sponsor: Rep. John Olumba

House Bill 5573 as introduced
Sponsor: Rep. Alberta Tinsley Talabi

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

House Bill 5575 (Substitute H-3)
Sponsor: Rep. Fred Durhal, Jr.

House Bill 5576 (Substitute H-2)
Sponsor: Rep. Joe Haveman

Committee: Detroit's Recovery and Michigan's Future
Complete to 5-22-14

A SUMMARY OF HOUSE BILLS 5566-5576 AS REPORTED FROM COMMITTEE

Brief Summary:

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 2014-15 through Fiscal Year 2034-35. (HB 5573)

- Create a 9-member Financial Review Commission, to include the state treasurer and director of the state DTMB, the mayor and city council president of the qualified city, and five gubernatorial appointees. The commission, among other things, would: 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 a higher amount as determined by the commission) 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 (except those approved by an emergency manager); and could file supplementary information relating the condition of the city with an arbitration panel in arbitration proceedings which the city is a party under Public Act 312 of 1969, which deals with compulsory arbitration of police and fire labor disputes.

Also the commission could, among other things: review, modify, 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, which could not be issued without commission approval; review compliance with deficit reduction plans; require the development and implementation of financial best practices; 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.)

- Require the commission to grant the city waivers from oversight if certain specified conditions are met and require 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 each fiscal year; 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 Financial Review Commission. The financial officer, among other things, would supervise all financial and budget activities of the city and coordinate the city's activities related to budgets, financial plans, financial management, reporting, and analysis. (HB 5567)

- Specify that, except as otherwise provided in a plan for adjustment, either of the following would apply to retirement benefits of employees first hired after July 1, 2023: (1) the city could offer retirement plans as long as the city does not contribute more than 7% of the employee's base pay to an appropriate retirement account; or (2) the city could offer the same retirement plan as provided in the plan for adjustment. (HB 5568)

- Stipulate that if the city provides retirement health care insurance benefits for new employees after July 1, 2023, the city could not contribute more than 2% of the employee's base pay, or the percentage that an employer contributes on behalf of a participant under Section 68b(1) of the State Employees' Retirement Act, whichever percentage is greater, to an appropriate tax-deferred account. No later than January 1, 2024, and each year thereafter, the city or a retirement system established by the city would have to submit a certificate of compliance to the Financial Review Commission. (HB 5568)

- Except as otherwise provided in a plan for adjustment, 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. (HB 5568)

- Prohibit, except as otherwise provided in a plan for adjustment, the annual pension benefit from including an additional payment based on the rate of investment return earned on the retirement system's assets. This would not prohibit the fulfillment of rights and benefits earned under a retirement system agreed to in a plan for adjustment. (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 or a new tax authorized unless the art institute was owned by a municipality on the date the tax levy or renewal was authorized. The millage would be limited to its current 10 years in duration (rather than the permitted 20 years). (HB 5571)

- Require Detroit's public employee retirement system to establish an investment committee, which would select and establish the compensation and terms of employment of the system's chief financial officer, as well as evaluate that CFO; restrict out-of-state travel of those affiliated with the system; and require reporting of out-of-state travel expenditures. The investment committee would also recommend to the governing board of the system various investment management decisions, as itemized in the legislation. These would include recommendations for the selection, monitoring, evaluation, and removal of custodians, investment managers, or investment service providers. (HB 5570)

- Define a "qualified city" as a city with a population of more than 600,000 that is subject to a plan of adjustment. A "plan for adjustment" refers to the plan for the adjustment of debts of a qualified city approved and entered by a U.S. bankruptcy court. (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.

HBs 5566 and 5567 would appropriate a total of $1.0 million in GF/GP revenue to the Department of Treasury. 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 Financial Review 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 limiting and potentially moving new employees into a new retirement system would depend on the precise provisions and associated normal costs of the retirement plans. For example, closing a defined benefit retirement plan (which the bills do not specifically require) generally 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 (unless the institute is owned by a municipality). This millage currently generates about $23 million in revenue per year.

<u>The Bills in Brief:</u>

The following bills are part of this proposed legislation.

<u>House Bill 5566</u> would create the Michigan Financial Review Commission Act. It also appropriates $900,000 from the General Fund to the Department of Treasury for commission resources in FY 2013-14; and contains a list of legislative findings and declarations as justification for the act.

<u>House Bill 5567</u> 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 each fiscal year; and to hold revenue estimating conferences each September and February. The bill also would allow the mayor of the city to veto a line item appropriating money in an appropriations ordinance; authorize the mayor, with the approval of the city council, to authorize reductions of line-item expenditures by executive order during a fiscal year if expenditures for the city exceed revenues; and require the city to post certain contracts on its website. The bill also contains a $100,000 appropriation to the Department of Treasury for the fiscal year ending September 30, 2015 (FY 2014-15).

<u>House Bill 5568</u> would amend the Home Rule City Act to address pension benefits and retiree health insurance, as described earlier in the summary. Those provisions would apply to "a city with a population of more than 600,000 or that has discharged $1 billion of pension liabilities in bankruptcy, or both."

<u>House Bill 5569</u> 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.

<u>House Bill 5570</u> would amend the Public Employee Retirement System Investment Act to require the city's retirement system to establish an investment committee, which would select and evaluate the system's chief financial officer (as described in more detail earlier); to restrict out-of-state travel of those affiliated with the system; and to require reporting of out-of-state travel expenditures. Under this bill, the retirement system is defined as a "large sponsored system"; that term refers to a system created and established by a city that is subject to a plan of adjustment and that meets one or more of the following conditions: (a) the city has a population of more than 600,000 or (b) the system has discharged at least $1 billion of pension liabilities in bankruptcy.

<u>House Bill 5571</u> would amend the Art Institute Authorities Act to prohibit the renewal of the existing voter-approved 10-year millage or the levy of a new millage unless the art institute was owned by a municipality on the date the tax levy or renewal was authorized.

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 2014-15 through Fiscal Year 2034-35.

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 this new authority could disburse the $194.8 million 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. If the conditions are not met, the money would be returned from the Settlement Administration Fund to the BSF.

The authority would have a three-member board chaired by the state treasurer. The other members would be the state budget director and a 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.

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

House Bill 5576 would amend Public Act 312 of 1969, dealing with compulsory arbitration of police and fire labor disputes, to correspond with provisions in House Bill 5566.

Summary of House Bill 5566:

The bill creates the Michigan Financial Review Commission Act. Under the new act, a nine-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 state treasurer
- The director of the Department of Technology, Management and Budget (or a designee)

- Three members appointed by the governor who have knowledge, skill, or experience in business or finance, with at least one being a resident of the city and at least one who is a state resident who is not a resident of the city.
- 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, and possess knowledge, training, skill, or experience in budgeting, actuarial science, law, or business operations.
- 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, and possess knowledge, training, skill, or experience in budgeting, actuarial science, law, or business operations.
- The president or chair of the city's governing body (the city council) or a designee.

Appointed members would serve four-year terms, although initial terms would be staggered. 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. A majority of members would constitute a quorum.

Most of the duties and powers of the commission are briefly described in the first paragraph (bullet point) of this summary. Generally, the commission, subject to a plan for adjustment and any collective bargaining agreements in effect, 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; 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 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, and to the mayor and governing body of the qualified city. The report also would have to be posted on the Department of Treasury website.

The commission would be required to grant the city <u>a waiver from one or more</u> of the requirements if it certifies that <u>all</u> of the following conditions are met:

- The commission certified that the city had adopted and adhered to deficit-free budgets for three consecutive years that comply with generally accepted accounting principles and are in accordance with the Uniform Budgeting and Accounting Act.

- The state treasurer and the city's chief financial officer certify that (1) all municipal securities or debt obligations sold by or for the benefit of the city in the general public market during the immediately preceding fiscal year and current fiscal year satisfied the capital and other financial requirements of the city during that period; and (2) 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 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.

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

- The city has established, as part of a system of employee compensation, retirement plans in which the qualified city contributes no more than 7% of an individual's base pay (excluding overtime, one-time lump sum payments, and the cost of fringe benefits) to an employee's retirement account.

- The city has implemented a program in which all contracts awarded are posted on the city's public website within 30 days of the contract award, including the identities of the parties to the contract, the dollar amount of the contract, and a brief description of the goods or services provided under the contract.

A waiver would be rescinded if the commission certified that any of the following, where applicable, have occurred or that there is a substantial likelihood that any will imminently occur:

- 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 Financial Review 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.
- 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 city has not met the retirement account requirements described earlier.

The commission could subsequently reverse the rescission of the waiver if it finds the circumstances that caused the rescission no longer exist.

The commission would have to dissolve itself if it has waived requirements, as described earlier, each year for the previous ten consecutive fiscal years and the plan for adjustment has expired. Its property, funds, and assets would be transferred to the state.

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■ 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.