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BILL ANALYSIS

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Senate Bills 846 through 856 (as introduced 10-25-07)
Senate Joint Resolution J (as introduced 10-25-07)
Sponsor: Senator Cameron S. Brown (S.B. 846 & 847 & S.J.R. J)
Senator John Pappageorge (S.B. 848)
Senator Randy Richardville (S.B. 849)
Senator Dennis Olshove (S.B. 850)
Senator Valde Garcia (S.B. 851 & 852)
Senator Hansen Clarke (S.B. 853)
Senator Tupac A. Hunter (S.B. 854)
Senator Buzz Thomas (S.B. 855)
Senator Mark C. Jansen (S.B. 856)
Committee: Homeland Security and Emerging Technologies

Date Completed: 11-6-07

CONTENT

Senate Bill 846 would create the "Divestment from Terror Act" to do the following:

- **Require a fiduciary (e.g., the State Treasurer with respect to various funds and retirement systems, or a community college board) to make its best efforts to identify all companies in which it had holdings that did business with or were located in a "state sponsor of terror" ("scrutinized companies") and create a list of those companies.**
- **Within 15 months, require a fiduciary to sell, redeem, divest, or withdraw all of the securities of a company that continued to have scrutinized active "business operations" (engaging in commerce with a state sponsor of terror).**
- **Except for indirect holdings in actively managed investment funds, prohibit a fiduciary from acquiring securities of companies on its list that had active business operations.**
- **Require a fiduciary to perform due diligence to prevent investment in any private equity fund invested in a scrutinized company with active business operations in a state sponsor of terror.**
- **If the manager of a publicly traded, actively managed fund in a fiduciary's portfolio created a similar fund not associated with scrutinized active business operations, require the fiduciary to replace its existing investments with investments in the new fund.**
- **Require the Department of Treasury to collect and publish on its website information regarding investments under the proposed Act, as well as the progress made in preventing new investment in scrutinized companies with active business operations in a state sponsor of terror and replacing existing investments.**
- **Exempt a fiduciary from any statutory or common law obligation that conflicted with the proposed Act.**
- **Provide immunity from liability for action taken to comply with the proposed Act.**

Senate Joint Resolution J would amend the State Constitution to prohibit public bodies from investing in entities engaged in business with known state sponsors of terror; and require public bodies to dispose of assets invested in such entities.

Senate Bills 847 through 856 would amend various statutes to require the applicable investment fiduciary to

comply with the proposed Divestment from Terror Act in making investments.

Senate Bill 847 would amend the Public Employee Retirement System Investment Act. Senate Bill 848 would amend Public Act 9 of the Extra Session of 1946, which governs the Veterans' Trust Fund. Senate Bill 849 would amend the Natural Resources and Environmental Protection Act with regard to the Environmental Protection Fund. Senate Bill 850 would amend the Community Colleges Act. Senate Bill 851 would amend the Michigan Strategic Fund Act. Senate Bill 852 would amend the Michigan Trust Fund Act with regard to the 21st Century Jobs Trust Fund. Senate Bill 853 would amend Public Act 249 of 1982, which governs the Children's Trust Fund. Senate Bill 854 would amend Public Act 105 of 1855, which governs the use and investment of surplus funds in the State Treasury. Senate Bill 855 would amend the Lottery Act with regard to the State Lottery Fund. Senate Bill 856 would amend the Michigan Education Trust Act.

Senate Bills 847 through 856 are tie-barred to Senate Bill 846. Senate Bill 846 and Senate Joint Resolution J are described below in further detail.

Senate Bill 846

Within 90 days after the proposed Act took effect, a fiduciary would have to make its best efforts to identify all scrutinized companies in which the fiduciary had direct or indirect holdings or could possibly have such holdings in the future. The efforts could include one or more of the following:

-- Reviewing and relying, as appropriate in the fiduciary's judgment, on publicly available information regarding companies with business operations in a state sponsor of terror, including information provided by nonprofit organizations, research firms, international organizations, and government entities.
-- Contacting asset managers contracted by the fiduciary that invested in companies with business operations in a state sponsor of terror.
-- Contacting other institutional investors that had divested from or engaged with companies that had business operations in a state sponsor of terror.
-- Reviewing the laws of the United States regarding the levels of business activity that would cause application of sanctions against companies conducting business or investing in countries that were designated state sponsors of terror.

"State sponsor of terror" would mean any country that the U.S. Secretary of State determined to have repeatedly provided support for acts of international terrorism.

("Fiduciary" would mean any of the following:

-- The Michigan Legislative Retirement System board of trustees for the Tier 1 plan for the Michigan Legislative Retirement System.
-- The State Treasurer for the retirement systems created under the State Police Retirement Act, the Judge's Retirement Act, the State Employees Retirement Act, and the Public School Employees Retirement Act.
-- The board of trustees of a community college.
-- The board of directors of the Michigan Education Trust.
-- The board of the Michigan Strategic Fund.

The term also would include the State Treasurer in connection with his or her duties under any of the following:

-- The Veterans' Trust Fund.
-- Public Act 105 of 1855.
-- The Children's Trust Fund.
-- The Lottery Act.
-- Section 503b of the Natural Resources and Environmental Protection Act (which Senate Bill 849 would add in relation to the Environmental Protection Fund).

"Scrutinized company" would mean any company that has business operations that involve contracts with or provision of supplies or services to a state sponsor of terror; a company in which a state sponsor of terror has any direct or indirect equity share, consortiums, or projects commissioned by a state sponsor of terror; or a company involved in consortiums and projects commissioned by a state sponsor of terror, to which one or both of the following apply:

-- More than 10% of the company's total revenue or assets are contributed directly or significantly to a state sponsor of

- terror and the company has failed to take "substantial action" (i.e., adopting, publicizing, and implementing a formal plan to cease scrutinized business operations within one year and to refrain from any new business operations).
- The company has, with actual knowledge, on or after August 5, 1996, made an investment of at least $20.0 million, or any combination of investments of at least $10.0 million each, that in the aggregate equal or exceed $20.0 million in any 12-month period, and that contribute directly or significantly to a state sponsor of terror, and the company has failed to take substantial action.

("Business operations" would mean engaging in commerce in any form with a state sponsor of terror, including by acquiring, developing, maintaining, owning, selling, possessing, leasing, or operating equipment, facilities, personnel, products, services, personal property, real property, or any other apparatus of business or commerce.)

At the end of the 90-day period or by the first meeting of a fiduciary following that period, the fiduciary would have to assemble all scrutinized companies identified into a scrutinized companies list. The fiduciary would have to update the list on a quarterly basis based on evolving information from, among other sources, those described in the bill.

The fiduciary immediately would have to determine the companies on the scrutinized companies list that the fiduciary oversaw pursuant to its responsibilities. If, within 90 days following the fiduciary's first engagement with a company, that company ceased scrutinized business operations, it would have to be removed from the list and the proposed Act would cease to apply to the company unless it resumed scrutinized business operations. If, within 90 days following the fiduciary's first engagement, the company converted its scrutinized active business operations to inactive business operations, the company would be subject to the Act.

("Active business operations" would mean all business operations that are not inactive. The term would not include the activities of any business, legal, or governmental entity or institution that provides humanitarian aid to the people of any state sponsors of terror. "Inactive business operations" would mean the mere continued holding or renewal of rights to property previously operated for the purpose of generating revenue but not presently deployed for that purpose.)

If, after 90 days following the fiduciary's first engagement with a company, the company continued to have scrutinized active business operations, and only while the company continued to do so, the fiduciary would have to sell, redeem, divest, or withdraw all of the company's publicly traded securities, according to the following schedule:

- Within nine months after the company's most recent appearance on the scrutinized companies list, at least 50% of the assets would have to be removed from the fiduciary's assets under management.
- Within 15 months after the company's most recent appearance on the list, 100% of the assets would have to be removed from the fiduciary's assets under management.

Except as provided below, at no time could the fiduciary acquire securities of companies on the scrutinized companies list that had active business operations.

This prohibition and the schedule for divestment would not apply to indirect holdings in actively managed investment funds. For purposes of this provision, actively managed investment funds would include private equity funds and publicly traded funds. Before the fiduciary invested in a new private equity fund that was not in its portfolio as of the proposed Act's effective date, the fiduciary would have to perform due diligence to prevent investment in any private equity fund where the offering memorandum or prospectus identified the purpose of the fund as investing in scrutinized companies with active business operations in a state sponsor of terror. The fiduciary would not be required to identify holdings in private equity funds or submit engagement letters to them. If the manager of a publicly traded, actively managed fund that was in the fiduciary's portfolio when the proposed Act took effect created a similar publicly traded, actively managed fund with indirect holdings devoid of identified scrutinized companies with scrutinized active business operations, the fiduciary would have to replace all applicable investments with investments in the similar fund in an expedited time frame consistent with prudent investment standards.

("Indirect holdings" of a company would mean all securities of that company held in an account or fund, including a mutual fund or other commingled fund, managed by one or more people not employed by the fiduciary, in which the fiduciary owns shares or interests together with other investors not subject to the proposed Act.)

Within one year after the proposed Act took effect, the Department of Treasury would have to collect and publish the following information on its internet website:

-- All investments sold, redeemed, divested, or withdrawn in compliance with the Act.
-- All prohibited investments made under the Act.
-- Any progress made in preventing new investment in private equity funds invested in scrutinized companies with active business operations in a state sponsor of terror, and the replacement of existing investments in publicly traded, actively managed funds.

Periodically, the Department would have to update the information at reasonable intervals.

With respect to actions taken in compliance with the proposed Act, including all good faith determinations regarding companies, a fiduciary would be exempt from any conflicting statutory or common law obligations, including any obligations with respect to choice of asset managers, investment funds, or investments for the fiduciary's securities portfolios.

A fiduciary, members of an investment advisory committee, and any person with decision-making authority with regard to investments of the fiduciary could not be held liable for any action undertaken for the purpose of complying with or executing the mandates of the proposed Act.

If any provision, section, subsection, sentence, clause, phrase, or word of the Act or its application to any person or circumstance were found to be invalid, illegal, unenforceable, or unconstitutional, it would be declared to be severable and the balance of the legislation would remain effective and functional notwithstanding the invalidity, illegality, unenforceability, or unconstitutionality.

Senate Joint Resolution J

Article VIII of the State Constitution provides for the University of Michigan board of regents, the Michigan State University board of trustees, and the Wayne State University board of governors, and requires that other institutions of higher education established by law having authority to grant baccalaureate degrees also be governed by a board of control.

Each board has general supervision of the institution and the control and direction of all expenditures from the institution's funds. Under the joint resolution, this provision would apply except as provided in Article IX, Section 19 (which prohibits the State from investing in stock, subject to exceptions).

The joint resolution would amend Article IX, Section 19 to prohibit a public body from investing or depositing any public funds in any business, legal, or governmental entity or institution that was engaged in business with known state sponsors of terror or that had facilities or conducted business in any state sponsor of terror. For the purposes of this provision, an independent franchise of a business entity would not be considered part of that business entity. This prohibition would not apply to the activities of any business, legal, or governmental entity or institution providing humanitarian aid to the people of any state sponsors of terror through a governmental agency or department or through a nongovernmental organization.

("Public body" would mean the State or a city, village, township, county, school district, public college or university, public community or junior college, or other governmental department, governmental agency, or political subdivision of this State. "State sponsor of terror" would have the same definition as proposed under Senate Bill 846.)

A public body would have to dispose of or withdraw any of its assets or money invested or deposited in a business, legal, or governmental entity engaged in business in or with a state sponsor of terror within the following time periods:

-- Within nine months after the joint resolution became part of the Constitution, at least 50% of those assets or money.
-- Within 15 months after the joint resolution became part of the Constitution, all of those assets or money.

The governing body of each public body annually would have to give the Department of Treasury any information concerning its compliance with Article IX, Section 19 that was required by law.

The joint resolution would have to be submitted to voters at the next general election, if two-thirds of the members elected to and serving in each house of the Legislature approved it.

MCL 38.1133 (S.B. 847)
MCL 35.605 (S.B. 848)
Proposed MCL 324.503b (S.B. 849)
MCL 389.124 & 389.142 (S.B. 850)
Proposed MCL 125.2007a (S.B. 851)
MCL 12.257 (S.B. 852)
MCL 21.171 (S.B. 853)
Proposed MCL 21.145 (S.B. 854)
MCL 432.41 (S.B. 855)
MCL 390.1429 & 390.1431 (S.B. 856)

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FISCAL IMPACT

The bills and joint resolution would have an indeterminate fiscal impact on State and local units of government. The Department of Treasury has explored the impact of these proposals with respect to its investments, which would not include all of the entities in the resolution and bills. For the Department's investments alone, Treasury has estimated that it would cost approximately $30,000 per year per country to ensure compliance with the proposed restrictions. That amount would cover the cost of hiring a private company to monitor compliance, and would be ongoing. There also could be additional up-front transaction costs to comply with these restrictions. The amount of those costs could be slightly lower for countries where the State has comparatively smaller investments. The Department has identified several countries that qualify as state sponsors of terror, including Sudan, Iran, North Korea, Syria, and Cuba, though that list is subject to change.

The fiscal impact on universities, community colleges, local units of government, and other public bodies is difficult to determine, as it would depend on the amount each entity has invested in relevant companies. The joint resolution would require that each public body report to the Department annually. While the resolution does not specify the Department's responsibility, if the Department of Treasury were charged with establishing a list of companies for each country and assisting public bodies with compliance, the Department would incur significant additional costs.

While it is difficult to quantify the precise fiscal impact of these bills on State and local government and other public bodies, it could be substantial. The Department of Treasury has indicated that not only would there be immediate transaction costs involved in the divestiture, there also would be compliance costs going forward as well. According to the Department, transaction costs could be considerable, particularly because these funds often invest in indices and mutual funds that contain many companies, which would make singling out individual companies more difficult. In addition to these more measurable costs, the Department predicts that the lost opportunity costs of prohibited investments could be high as well, thereby affecting the overall value of State investments; however, these potential costs or gains could only be determined retrospectively.

As of September 30, 2006, the State Employees' Retirement System, Public School Employees' Retirement System, State Police Retirement System, and Judges Retirement System had combined total assets of approximately $64 billion.

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