

Legislative Analysis



DETROIT BANKRUPTCY-RELATED PACKAGE

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House Bills 5566 & 5600 as enacted
Public Acts 181 & 190 of 2014
Sponsor: Rep. John Walsh

House Bill 5567 as enacted
Public Act 182 of 2014
Sponsor: Rep. John Kivela

House Bill 5573 as enacted
Public Act 186 of 2014
Sponsor: Rep. Alberta Tinsley Talabi

House Bill 5568 as enacted
Public Act 183 of 2014
Sponsor: Rep. Gail Haines

House Bill 5574 as enacted
Public Act 188 of 2014
Sponsor: Rep. Thomas F. Stallworth III

House Bill 5569 as enacted
Public Act 184 of 2014
Sponsor: Rep. Andrea LaFontaine

House Bill 5575 as enacted
Public Act 187 of 2014
Sponsor: Rep. Fred Durhal, Jr.

House Bill 5570 as enacted
Public Act 185 of 2014
Sponsor: Rep. Ken Yonker

House Bill 5576 as enacted
Public Act 189 of 2014
Sponsor: Rep. Joe Haveman

Committee: Detroit's Recovery and Michigan's Future
Complete to 6-25-14

A SUMMARY OF HOUSE BILLS 5566-5570, 5573-5576, & 5600 AS ENACTED

Brief Summary:

Generally speaking, this package of bills does the following:

- Authorizes 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 to a newly-created fund administered by a Settlement Administration Authority, and then paid to the retirement systems if certain conditions are met. (HB 5574 and HB 5575)
- Requires 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)
- Creates 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 to 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 created a new act establishing this commission and is described in more detail later.)

- Requires the commission to grant the city waivers from oversight if certain specified conditions are met, and requires the commission to dissolve itself under specified circumstances (as detailed later in the description of HB 5566).
- Requires 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 is to 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, is to 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)
- Specifies that, except as otherwise provided in a plan for adjustment, either of the following applies 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)
- Stipulates that if the city provides retirement health care insurance benefits for new employees after July 1, 2023, the city cannot 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)

- Restricts the calculation of a pension benefit under a defined benefit plan to include only base pay; this does 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 applies as of January 1, 2015, and applies "except as otherwise provided in a plan for adjustment." (HB 5568)
- Prohibits, 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)
- Limits 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)
- Requires 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)
- Defines a "qualified city" as a city with a population of more than 600,000 that is subject to a plan for 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 under Chapter 9 of Title 11 of the United States Code. (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 transferring \$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 \$581.1 million at the close of FY 2013-14. The bills would reduce that balance to approximately \$386.3 million.

The appropriation amount of \$194.8 million 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 enacted budget reserved (that is, does 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.

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.

The Bills in Brief:

The following bills are part of this proposed legislation.

House Bill 5566 creates 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. A more detailed description of the bill can be found later in the summary.

House Bill 5567 amends 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 all contracts on its website within 30 days. The bill also contains a \$100,000 appropriation to the Department of Treasury for the fiscal year ending September 30, 2015 (FY 2014-15).

House Bill 5568 amends 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."

House Bill 5569 amends 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 amends 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 for 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.

House Bill 5573 amends 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 amends the Management and Budget Act to transfer \$194.8 million from the BSF to the Settlement Administration Fund.

House Bill 5575 creates the Michigan Settlement Administration Authority Act. Under the act, this new authority would 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 for the adjustment of debts for the city; and (2) the terms and conditions of the contribution agreement (within the plan for adjustment) have been satisfied. If the conditions are not met, the money would be returned from the Settlement Administration Fund to the BSF.

The authority has a three-member board chaired by the state treasurer. The other members are 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 lengthy 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 amends Public Act 312 of 1969, dealing with compulsory arbitration of police and fire labor disputes, to correspond with provisions in House Bill 5566.

House Bill 5600 amends Public Act 566 of 1978, which prescribes standards of conduct for public officers and employees and prohibits the holding of incompatible offices. The bill specifies that serving as a member of the Financial Review Commission that will be established for the City of Detroit is not incompatible with serving as the mayor, chief executive officer, or member of the governing body (city council) of that city.

Summary of House Bill 5566:

The bill creates the Michigan Financial Review Commission Act. Under the new act, a nine-member commission is to 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 nine 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 must be a city resident and all must have 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 must be a city resident and all must have 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 serve four-year terms, although initial terms are to be staggered. The commission must meet at least monthly, and meetings are 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 are subject to the Freedom of Information Act. A majority of members constitutes 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, must 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 is also charged with ensuring that the city complies with provisions in the Revised Municipal Finance Act and the Uniform Budget and Accounting Act, as well as with the various amendments to state statutes made by the other bills in the package of legislation.

The city would written reports to the commission when so required regarding its financial stability and must 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 is required to grant the city a waiver from one or more of the requirements if it certifies that 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 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 within 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.