

RETIREMENT SYSTEM INVESTMENT REVISIONS

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Senate Bill 797

Sponsor: Sen. Jansen

House Committee: Appropriations

Senate Committee: Appropriations

Complete to 8-10-12

A SUMMARY OF SENATE BILL 797 AS PASSED BY THE SENATE 5-29-12

Senate Bill 797 would amend the Public Employee Retirement System Act to make a series of revisions to provisions governing how state and local retirement system assets are invested. Changes to limitations on retirement system investments in various categories under the bill are as follows:

- Adds global security equity positions to the domestic stock category that is limited to 70% of system assets and clarifies that investments may be made in global securities registered on an industry-recognized system outside the United States.
- Limits investments in "obligations" (bonds, notes, etc.) outside of categories specified in the act to no more than 15% of total system assets, replacing current provisions related to the ratio between net earnings and fixed charges for such obligations.
- Increases, from 5% to 10%, the percentage of system assets that may be invested in real estate investment trusts. Also increases, from 5% to 10%, the percentage of assets that may be invested in real or personal property. (Investments in those categories could exceed 10% if the State Treasurer is the investment fiduciary for the system.)
- For systems for which the State Treasurer is not the investment fiduciary and that have assets of \$1.0 billion or more, establishes a limit of 10% for the percentage of system assets that could be invested in private equity. Allows an additional 5% of assets of such systems to be invested in Michigan private equity. For systems with assets between \$250.0 million and \$1.0 billion, the bill would limit investments in Michigan private equity to 5% of system assets. (Currently, the act only specifies a limit on private equity investments for systems in which the State Treasury is the investment fiduciary, with a limit of 30%.)
- Increases the limit for the percentage of system assets that may be invested in investments not described in a category elsewhere in the act as follows:
 - For a system with assets below \$250.0 million: from 5% to 15%.
 - For a system with assets of between \$250.0 million and \$1.0 billion: from 10% to 20%.
 - For a system with assets of \$1.0 billion or more: from 15% to 25%.
 - For a system for which the investment fiduciary is the State Treasurer: from 20% to 30%.

- Increases the limit for the percentage of system assets that may be invested in global securities, for a system for which the investment fiduciary is the State Treasurer or a system with assets of \$2.0 billion or more, from 20% to 30%.

Other significant changes included in the bill are as follows:

- Replaces the term "foreign security" with "global security."
- Specifies that the term "investment fiduciary" applies to the State Treasurer for state retirement systems (the State Employees', Judges', State Police, and Public School Employees' systems).
- Revises the definition of the term "investment" to exclude, as a sole investment, a pledge of the system's assets as collateral to guarantee the repayment of obligations made by a third party to a borrower.
- Requires that a retirement system's investment fiduciary prepare written policies regarding ethics and professional training and education.
- Requires that a retirement system's investment fiduciary publish an annual report that includes information on the system's investment fiduciaries and service providers, the system's assets and liabilities, the system's funded ratio, the system's investment performance net of fees for various specified time periods, the system's administrative and investment expenditures (including soft dollar expenditures and professional training/education expenditures), the system's itemized budget, and various data on system participation, performance, and actuarial methods. The system would be required to make the report available to participants, beneficiaries, and the public, and post the report on its website.
- Clarifies the purposes for which system income may be used. Those purposes would include costs of professional training and education (including travel costs) of system board members if the training and education are directly related to the management of the system. Limitations would be placed on total professional training and education costs (including travel costs) for a system:
 - \$150,000 or \$12,000 times the number of system board members, whichever is less, for total costs in a fiscal year.
 - \$30,000 for costs for an individual board members in a fiscal year.
 - Those limitations would be adjusted annually for inflation.
- Requires full disclosure by investment service providers of all fees or other compensation associated with its relationship with the retirement system, both before and after (on an annual basis) investment services are provided.
- Prohibit payment to a service provider if the service provider or a "covered associate" of the service provider (as defined in the bill) has made a contribution to an official of a governmental entity during the preceding 24-month period (beginning only after the date the bill took effect) for any of several specified election-related purposes. Exceptions would be made if the individual making the contribution was eligible to vote for the official (limit of \$350 per election), if the contribution did not exceed \$150 per election, if the contribution was made more than 6 months prior to an individual becoming a covered associate, or if a contribution was made but returned within certain time limits (limit of \$350). Officials included under this prohibition are holders or candidates for an office that can influence the outcome of hiring a service

provider by a system or that has the authority to appoint an individual who can influence the hiring of a service provider by a system.

- Provides for an investment fiduciary or service provider convicted of or entering a no contest plea for a felony or misdemeanor arising out of his or her service to a retirement system to reimburse the system for all costs, including legal defense fees, that were paid by the system.
- Clarifies the types of investment companies in which investments may be made (those in which investor liabilities do not exceed the amount of the investment).
- Adds provisions regulating the investment of funds in a collective investment fund, common trust fund, or pooled fund.
- Requires a retirement system to retain its financial records for a minimum of 6 years from the date the record was created, exempts information regarding the calculation of retirement benefits for system members from disclosure under the Freedom of Information Act, and provides for the system to provide a requesting political subdivision with a reasonable opportunity to inspect information regarding the calculation of retirement benefits for system members (subject to possible confidentiality requirements and fees and expenses to be paid by the subdivision).
- Specifies benefits to be included in a system's annual actuarial valuation and provides that system assets may not be used to conduct the supplemental actuarial analysis conducted prior to adoption of pension benefit changes, as required under section 20h(5).
- Allows for a governing board of a retirement system to remove a member of the board by a unanimous vote of the other members of the board, by an order of a circuit court, or by the process contained in the system's plan provisions. Provisions would be added specifying the reasons for which a board member could be removed and governing the processes for holding a hearing on the removal, replacing a removed member, and appealing the removal of a member to the circuit court or other appropriate court (with individuals seeking the removal of a member subject to paying the cost of the proceedings in the case in which a the court found that the petition for removal was filed in bad faith).

FISCAL IMPACT:

The bill would have no direct fiscal impact on state or local government. Financial implications for retirement systems governed by the act would depend on investment decisions made under the new provisions and subsequent investment returns. The additional reporting requirement contained in the bill may create some administrative costs for state and local retirement systems, which should generally be minimal relative to system assets.

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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.