Legislative Analysis

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MUNICIPAL BONDS FOR UNFUNDED LIABILITY OF RETIREMENT & HEALTH CARE BENEFITS

House Bill 6694
Sponsor: Rep. Dave Hildenbrand
Committee: Local Government and Urban Policy

Complete to 12-4-06

A SUMMARY OF HOUSE BILL 6694 AS INTRODUCED 11-30-06

The bill would amend the Revised Municipal Finance Act to permit local governmental units to issue municipal securities (bonds) to pay the costs of the unfunded actuarial liability of a public employee retirement system pension plan or of other post-employment benefits, such as health benefits.

The bill would apply to a county, city, village, township, school district, intermediate school district, or community college district. Securities could be issued by resolution of the unit's governing body and without a vote of electors. They would be secured by the full faith and credit of the local unit.

Unfunded Actuarial Liability. The term "unfunded actuarial liability" would be defined to mean the amount by which a fund is short of the amount necessary to pay retirement or other post-employment benefits to beneficiaries and participants of a public employee retirement system or post-employment benefit system. (The amount would have to be calculated in accordance with the standards of practice promulgated by the Actuarial Standards Board of the American Academy of Actuaries.)

Tax Limitations. The bill would specify that the amount of taxes needed to pay principal and interest on such securities, together with other taxes levied, could not exceed limits authorized by law.

Notice of Issuance. Before issuing a municipal security, the governmental unit would have to publish a notice of intent, directed at the voters of the appropriate local unit and published in a newspaper with general circulation in the local unit. The notice would have to state the maximum amount of securities to be issued; the purpose; the right to a referendum on the issuance; and any other information needed to adequately inform voters of the nature of the issue.

Right of Referendum. If at least 10 percent of registered voters (or 15,000 voters, whichever is less) sign a petition requesting a referendum and file it with the local governing body within 45 days after the notice is published, then a referendum would have to be held before securities could be issued. A majority vote of electors at a general or special election would be required to issue securities. (A special election held for this purpose would not be included in statutory or charter limitations on the number of special elections that can be held.)

Comprehensive Plan of Finance. Before issuing municipal securities under the bill, a local unit would need to prepare a comprehensive plan of finance indicating its ability to manage its unfunded actuarial liability. The plan would have to include (1) documentation that proceeds from issued securities and annual required contributions will be adequate to meet the level of benefits provided; (2) an amortization of unfunded liabilities and a description of actions to accomplish the amortization; (3) a description and explanation of any and actuarial assumptions; (4) a schedule illustrating the amortization of unfunded liabilities; (5) a comparative review illustrating the level of funds available to the plan from rates, investment income, and other sources covered over the period covered by the plan with the rates used; (6) a statement certified by an actuary within 36 months prior to the issuance date of the securities that the plan is complete and accurate; and (7) demonstration that the issuance of securities will result in a projected present value savings based on the amortization schedule discounted at the true interest cost of the total amount borrowed when compared to the actuarial assumption related to the rate of return on plan assets.

Characteristics of Securities. Other provisions that apply to the municipal securities issued under the bill include:

-- The maximum term would be 30 years.

-- They would need to have been assigned an investment grade by at least one nationally recognized rating agency.

-- They could not exceed five percent of the state equalized valuation (SEV) of the property in the local unit.

-- Up to 50 percent of the principal amount of any security issued could be sold at a discount exceeding 10 percent.

-- They could mature annually or be subject to mandatory redemption requirements, with the first annual maturity or mandatory redemption requirement to fall due five years or less from date of issuance, and some principal amount would have to mature or be subject to redemption in each subsequent year of the term of the security.

-- Securities could not on a cumulative basis exceed 75 percent of current unfunded actuarial liabilities.

-- Proceeds from securities would have to be deposited in a special fund and could be invested as allowed under the Public Employee Retirement System Investment Act.

MCL 141.2103

FISCAL IMPACT:

The bill may increase the short term revenue of local units of government by permitting bonding through the use of general obligation bonds to pay the cost of unfunded public employee pensions and other post-retirement benefits, such as health care. The Michigan Municipal Employees Retirement System (MERS) reports that its 644 local government participants collectively owed $1.6 billion in unfunded actuarial accrued pension liabilities as of December 31, 2005. Of course, this short term revenue increase will result in higher future debt service payments to retire any such bonding for up to 30 years, which is the maximum term allowed under this bill. The proceeds of such bonds must be invested as provided for in the Public Employee Retirement System Investment Act.

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