

**SENATE FISCAL AGENCY  
 MEMORANDUM**

**DATE:** October 5, 2018  
**TO:** Members of the Michigan Senate  
**FROM:** Michael Siracuse, Fiscal Analyst  
 Kathryn Summers, Associate Director  
**RE:** Executive Order 2018-10

**Executive Order 2018-10**

On September 27, 2018, Governor Snyder issued Executive Order (E.O.) 2018-10, which created the Michigan Investment Board (Board) within the Department of Treasury. The Executive Order assigned to the Board the duties and responsibilities of investment fiduciary for the State's Retirement System, and transferred all of the powers, duties, functions, and responsibilities of the State Treasurer under Act 314 of 1965, to the Board. In addition, the E.O. transferred all of the powers, duties, functions, and responsibilities of the Investment Advisory Committee to the Board and further abolished that committee.

Article V, Section 2 of the Michigan Constitution states that the Legislature has 60 calendar days following the issuance of an Executive Order to disapprove it; the last day for the Legislature to reject E.O. 2018-10 is Monday, November 26, 2018.

**Overview**

Prior to the E.O., the State Treasurer and the Investment Advisory Committee (IAC) were responsible for the investment and management of the State of Michigan Retirement System (SMRS) for state employees, including management of defined benefit plans, defined contribution plans, the Military Retirement System, and other post-employment benefits (OPEB). The State Treasurer had the primary duty to act as fiduciary for the SMRS and to make investment decisions. The IAC, a five member committee made up of the Director of Licensing and Regulatory Affairs (LARA) (or designee), the Director of the Department of Technology, Management and Budget (or designee), and three Governor-appointed public members, had the power to review investments, make recommendations, and, more specifically, direct the Treasurer to dispose of holdings by majority vote and direct the Treasurer to make a specific investment by unanimous vote. The new Board will change this dynamic.

Under the E.O., the new Board will assume all of the fiduciary and investment duties with regard to the SMRS previously held by the Treasurer and the IAC. The State Treasurer will chair the Board, and the State Budget Director also will be a member, along with three public members appointed by the Governor who are qualified via experience or knowledge in investment and or pension administration. The public members will serve without pay. The terms of the appointed members are for four years, but at the creation of the Board, the first terms of the appointed members will be staggered at two, three, and four year terms. Public members may serve up to two consecutive full terms, with no member serving more than 10 years. Public members also must meet eligibility requirements, and may be removed if charged or convicted of a fraudulent crime. A public member

also may be removed if he or she sustains a civil judgement for a breach of fiduciary duties, is sanctioned by the Securities and Exchange Commission, or otherwise becomes conflicted due to an employment or financial obligation of the public member (or a member of his or her family) to a service provider to the retirement system or the Bureau of Investments.

The E.O. requires that the new Board meet quarterly at public meetings in compliance with the Open Meetings Act, 1976 PA 267. Additional meetings may be called by the State Treasurer, as chairperson. The purpose of the meetings is to perform the duties of the fiduciary to the SMRS, as previously assigned to the State Treasurer under Act 314, including the review of reports on investment performance, approval of an investment policy statement, and approval of Tier 1 investment targets every two years. The Board also will be required to adopt and approve ethics rules for its members to be posted on the Bureau of Investments website. The Board also will have the power to appoint a Chief Investment Officer, whenever the position is vacant, to manage the day-to-day investment operations functions of the Bureau of Investments.

The E.O. prescribes the powers and duties under Act 314 to the Board. As specified in the E.O., this includes the fiduciary duties to act as the custodian for the Retirement System's assets and the investment of those assets through the Bureau of Investments. This also means the Board may sue and be sued in matters arising out of its fiduciary responsibilities specifically to those assets.

The new Board also will direct the activities of the Bureau of Investments, including the collection of principle and interest for the Retirement System, accounting for income and expenses of the Retirement System, expending appropriated funds for the support of the Board and for the development, professional dues, and expenses for Bureau of Investments staff, exercising shareholder rights regarding investments, and the negotiation, selection, and retention of investment managers, service providers, consultants, and other services related to the Retirement System.

The E.O. specifically states that the Board is authorized to invest the Retirement System's assets, and that the Retirement System includes Tier 1 plans (defined as defined benefit retirement plans for Public School employees, State employees, State Police, and Michigan judges), the Military Retirement System (which provides payments to qualified veterans under the Michigan Military Act, 1967 PA 150, and the Military Establishment Act, 1909 PA 84), and OPEB.

Lastly, the E.O. states that existing rules, orders, contracts, plans, investments, agreements and lawfully-commenced lawsuits in which the Department or Bureau is a party, shall continue to be effective and not disrupted by the creation of the new Board and the transfer of authority to it from the State Treasurer or the Investment Advisory Committee.

### **Transfer of Powers under the Public Employee Retirement System Investment Act**

As per the E.O., the Board is created within the Department of Treasury and the Board assumes all of the responsibilities and duties of the State Treasurer under Act 314. Act 314, as referred to in the E.O., is the Public Employee Retirement System Investment Act (MCLs 38.1121 through 38.1141). The Act authorizes the investment of the assets of the public employee retirement systems, provides for the payment of investment-related expenses, authorizes investment in variable rate interest loans, defines and limits investments of the retirement system, and prescribes the powers and duties of investment fiduciaries, departments, and officers.

Also pursuant to the E.O., the Investment Advisory Committee, which had the power to direct the State Treasurer to dispose of an investment with a majority vote or make an investment with a unanimous vote, is abolished. The members of the IAC were three public members appointed by the Governor, as well as Shelly Edgerton, current Director of LARA, and Phillip Stoddard, past Director of the Office of Retirement Services in the Department of Technology, Management and Budget. The new Board also will have three public members, but will not include the Directors of LARA and DTMB (or designees). It will include the State Treasurer, as Chairperson, and the State Budget Director, currently John Walsh of DTMB. It is not known whether the three public members previously appointed to the IAC will serve on the new Board. The E.O. also specifies that the Treasurer and State Budget Director must serve on the new Board without designee.

This means that power to manage the investments for the entire SMRS, including the Military Retirement System and OPEB, is moving, essentially, from the Treasurer to the new Board. Previously, the Investment Advisory Committee could overrule or direct the State Treasurer regarding a particular investment with a majority or unanimous vote, respectively. The structure of this arrangement via the new Board will be slightly different. The State Treasurer can still direct the Bureau of Investments to manage the assets of the SMRS, but will now need approval from the new Board to do so. It is worth noting that the State Treasurer will be the chairperson of the Board under the E.O., which is silent as to how approval is granted for asset strategies or investment, but it may be a reasonable assumption that a majority vote would be required for such general approval, or for approval or rejection of specific investments or investment strategies.

The abolished Investment Advisory Committee was created to review SMRS investments, make recommendations, and, if necessary, overrule an investment decision of the State Treasurer or direct the State Treasurer to make a specific investment. These specific powers are transferred to the new Board created by the E.O.

The guidelines and limitations by which SMRS investments and assets are to be managed will remain unchanged. Those are found in Act 314, which the E.O. specifies will now apply to the Board instead of the State Treasurer.

### **Types of Transfers**

Article V, Section 2 of the State Constitution authorizes the Governor to organize the Executive branch of government by Executive Order. Three types of reorganizations are identified in the Executive Organization Act:

**Type I Transfer.** Under a Type I transfer, an existing department, board, commission, or agency is transferred intact to another principal department. The entity is administered under the supervision of the new principal department; however, the prescribed statutory powers, duties, and functions are exercised by the entity as a relatively autonomous entity.

**Type II Transfer.** Under a Type II transfer, all of the statutory authority, powers, duties, and functions, as well as records, personnel, property, unspent balances of appropriations and other funds associated with an entity, and the entity itself, are transferred to and placed under the authority of the principal department.

**Type III Transfer.** A Type III transfer abolishes an existing entity. The statutory authority, powers, duties, functions, records, personnel, and funding are not abolished, but are transferred to a principal department."

The E.O. abolishes the Investment Advisory Committee and transfers all of its authority, functions, personnel, and funding to the newly created Board housed within the Department of Treasury. The E.O. does not specify whether this transfer is a Type I, II, or III transfer, but it appears to be a Type III transfer. The statutory language that created the Investment Advisory Committee, MCL 16.191, is found under Chapter 4 of the Executive Organization Act, titled "Department of Treasury"; however, that language did not specifically place the Committee with that, or any other, Department.

### **Fiscal Impact**

Executive Order 2018-10 would not have any impact upon the State or local units of government. The only possible cost would be the reimbursement of travel and expenses for the three public members appointed by the Governor to the Board; however, as these expenses were also included in the cost of the three public members of the IAC which the E.O. abolishes, the cost/savings for travel and related expenses is likely to be net zero.

### **Summary**

E.O. 2018-10 will replace the five-member Investment Advisory Committee with the five-member State of Michigan Investment Board, created in section II of the order. The new Board will not include the Directors of LARA or DTMB, but will, instead, include the State Treasurer and the State Budget Director. It is not known if the three current public members of the IAC will be appointed to the new Board, or if new public members will be named by the Governor.

In addition to transferring the powers and duties of the IAC to the Board, the E.O. also transfers the fiduciary duties and responsibilities of the State Treasurer with regard to the State's Retirement Systems to the new Board. The new Board will now be responsible for management of those systems, which include the Defined Benefit plans, Defined Contribution investment plan selection, the Military Retirement System, and OPEB.

Executive Order 2018-10 will take effect on November 26, 2018, unless the Legislature rejects it before that date.

If you have any questions on E.O. 2018-10, please do not hesitate to contact us.

/lms

c: Ellen Jeffries, Director