The Detroit News

Wednesday, March 4, 2015 | detroitnews.com

Retiree costs force Macomb gamble

County, like others, is borrowing money to pay rising legacy tab

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Lansing — Macomb County intends to sell $263.7 million in bonds next week to finance its unfunded retiree health care bill, making it the 11th local government in Michigan to gamble on investments to help pay for and contain rising legacy costs.

Since 2013, localities as small as Bloomfield Hills and as large as Oakland County have used a little-known state law to float a combined $711 million in bonds to aid retiree health care and pension plans. Macomb County's sale would bring the total to nearly $1 billion borrowed to infuse cash into retired worker trust funds.

The cities, townships and counties are betting they can make more money in stocks and other investments than by paying fluctuating retiree health care benefits and pension contributions as they go. In doing so, they lock in annual fixed costs for former workers.

It's a strategy similar to one former Detroit Mayor Kwame Kilpatrick's administration pursued in 2005, when the city borrowed $1.44 billion to prop up its ailing pension funds — a complex deal that later would contribute to the city's 2013 bankruptcy.

"I think Detroit shows you exactly what can go wrong with these things," said Eric Scorsone, an economics professor and municipal finance expert at Michigan State University. "There's no financial instrument out there that's risk-free."

Officials in Macomb County and other local governments argue their borrowing plans are far less risky than Detroit's scheme, which was fraught with a complicated interest payment and a series of trusts that critics said were designed to bypass statutory debt limits.

To borrow the money, the state law requires municipalities to close their pension and retiree health care plans to new hires — a reform Detroit did not pursue until it ended up in bankruptcy court.

"We wouldn't even be considering this if the plan wasn't 100 percent closed, unlike Detroit ... which spent millions and millions to shore up their liability, but never closed the plan," said Mark Deldin, deputy executive of Macomb County.

Macomb County hopes to sell investors bonds Tuesday at an interest rate of 3.5 percent or lower, Deldin said, meaning its investments will have to exceed that rate over the 24-year life of the bonds for the county to come out ahead.

"We would be foolish not to take advantage of it, especially in today's bond market with interest rates being so low," he said. "There's always risk in anything

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you do when it comes to that. No one can predict what the stock market is going to do."

Borrowing money to pour into pension funds dates back 30 years among local and state governments, according to the Center for Retirement Research at Boston College.

But issuing new debt to pay for retiree health care — known as other post-employment benefits — is "very rare" among municipalities across the country, said Matt Fabian, a partner at Municipal Market Analytics, a Concord, Mass.-based bond research firm.

Fabian said he is alarmed by the increasing use of bonds for health care obligations among Michigan communities and counties.

"It's like paying off one credit card with another," he said. "And it is a gamble with taxpayer dollars."

In Oakland County, the gamble paid off, according to Deputy County Executive Robert Daddow.

In 2007, Oakland Executive L. Brooks Patterson's administration borrowed $557 million to fully fund the county's retiree health care tab. Oakland County refinanced the debt in 2013 at $350 million after its health care trust fund's investments increased the value of the borrowed money to 128 percent, Daddow said.

"If the market drops 28 percent, I'm still fully funded, but I can tell you there's going to be a lot of other folks sucking wind," Daddow said. "We made a killing here. Have you ever bet half a billion (dollars) in your life?"

Despite Oakland County's investment gains in recent years, Fabian and other analysts questioned why Michigan municipalities are borrowing money now to invest when the value of stock indexes are reaching all-time highs.

"As a laymen looking at the market today, you might think this may not be the best time to issue a (pension bond)," said Jean-Pierre Aubry, assistant director for state and local research at the Center for Retirement Research.

The 10 other local governments that have issued bonds to fund their pensions and retiree health care obligations have used a 2012 law, which was extended in December by one year.

Under the law, each municipality must have a minimum double-A credit rating and can use the bonds only to pay off an accrued unfunded liability for a pension or retiree health care plan that's no longer offered to current workers.

Local governments have issued bonds for the legacy costs under different circumstances.

Shelby Township bonded $9.3 million and borrowed $24 million from its public works department's reserve fund to help close off its pension plan, Supervisor Richard Stathakis said.

"Without fixing this pension problem, this budget would not be sustainable," Stathakis said.

Allegan County borrowed $15 million, locked in its annual payments at $1.1 million and saved the west Michigan county $11 million in long-term added costs for having an underfunded retiree health care account, Administrator Rob Sarro said.

"Had we not bonded, there would have been some years where that payment would have grown to $2.5 million in a single year, which as you could imagine could put a big strain on your ($30 million) general fund budget," Sarro said.

State Sen. Jack Brandenburg, R-Harrison Township, is sponsoring a bill this year to extend the program another four years through 2020 that the Senate plans to vote on Wednesday.

Brandenburg said the program ensures municipalities "meet their obligations" every year with required payments.

"When it comes right down to it, there's a hell of a temptation not to fund and let it slide for a year," Brandenburg said. "There really is no logical answer why somebody wouldn't take advantage of this. It's cheap money."