Pontiac leaders draw battle lines over state oversight exit
by Andrew Scurria and Gunjan Banerji
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The **City of Pontiac**'s branches of government are at loggerheads over how to leverage an overfunded pension system in its quest to exit receivership, said City Administrator Joseph Sobota.

Pontiac's General Employees Retirement System (GERS) added USD 221.6m to the city's unrestricted net position in FY15, according to its most recent comprehensive annual financial report (CAFR). Due to underfunding, most cities' net positions decreased under new Governmental Accounting Standards Board (GASB) accounting rules that kicked in last year, but not Pontiac's.

The city was one of the few to benefit from the adoption of GASB Statement 68, a rule allowing issuers to book excess pension assets on citywide financial statements.

"If you look at government-wide numbers for all cities in Oakland County, Pontiac has the highest unreserved net assets," Sobota said.

GERS boasted a 182% funding ratio as of 30 June 2015, the city reported. Somewhat offsetting that pension surplus, however, is the city's retiree healthcare liabilities, commonly called other post-employment benefits (OPEBs). Pontiac public safety personnel who retired after 1996 participate in a tax-exempt voluntary employees' beneficiary association (VEBA) that effectively closed to new entrants in 2012. Pontiac also sponsors a general employees' retiree health care plan, perhaps the largest variable in the city's budgetary picture.

Funded on a pay-as-you-go basis, the retiree health care plan was underfunded by USD 181.2m as of 31 December 2014, according to Pontiac's FY15 CAFR. The city also ran up a USD 44.6m net OPEB obligation in FY15.

Banking on emergency manager cuts

Those numbers assume that former Emergency Manager Louis Schimmel's elimination of general retiree health and dental insurance stand up to legal challenge. Sobota estimates that the health care modifications, which went effective 1 September 2013, after the **State of Michigan** enacted the Public Act 436 emergency management law, have saved the city USD 10m-12m annually. In FY13, Pontiac spent USD 13.5m on insurance coverage, of which USD 1.2m was for active employees. In FY15, the figure was USD 1.7m.

The city has been in court-supervised mediation over those OPEB modifications for nearly a year now. The Pontiac Retired Employees Association sued in federal court, claiming that the modifications unconstitutionally impaired benefits they were promised under prior collective bargaining agreements.

The employees failed to win an injunction at the trial court level, but after a rare hearing before the full bench of the Sixth Circuit appeals remanded the case back with instructions for the presiding judge to conduct fact-finding.

The docket shows no further activity since February 2015. The city’s attorney did not return a request for comment.

By the time of the appellate ruling, Pontiac had exited emergency management in favor of receivership and is currently under the supervision of a Receivership Advisory Transition Board (RTAB) tasked with assessing the city’s financial progress. Last week, state officials working for the RTAB recommended “a reduced degree of oversight,” according to a Michigan Treasury Department spokesperson.

“Pontiac has come a long way since ’08,” said Patrick O’Keefe, a Michigan-based restructuring advisor at a firm with his namesake. The city rightsized its balance sheet by sharing and consolidating services with neighboring municipalities, a strategy several Michigan municipalities have employed in face of unfavorable demographics, he said. That included selling sewer system operations to Oakland County for USD 55m, as reported.

The evaluation noted that total fund balance in the general fund was USD 10.8m as of the FY15 close; the unassigned fund balance was USD 9.9m. The next step on Pontiac’s road back to self-governance is for the RTAB to consider a recommendation to the state treasurer to reduce oversight, the spokesperson said.

Pontiac’s long-term debt profile depends on the fate of its Tax Increment Financing Authority (TIFA) component unit, which issued USD 29m in property tax-backed bonds in 2007. The city guaranteed the bonds, which had USD 24.9m in principal outstanding at the FY15 close. When TIFA’s property tax collections were insufficient to pay debt service in FY15, the city’s general fund paid USD 575,000 to bondholders because of the guaranty.

The shortfalls in TIFA debt service are expected to continue. TIFA is required to reimburse the city for the shortfall with future revenues when they are available, but Pontiac does not anticipate that happening “in the near future,” its audit said. Pontiac estimated that it ultimately will pay another USD 7.37m on the guaranteed bonds, representing the discounted present value of future general fund debt service payments.

Ball lands in Michigan’s court

The overfunding in GERS may give Pontiac a chip in this dance with the state. Sobota has been an advocate of merging GERS with the state Municipal Employees Retirement System (MERS), which he said would allow for seizing some of the plan surplus.

MERS requires that new plans enter with at least 120% of the assets needed to fund promised benefits; assets above 130% can be returned to the plan sponsor. In Pontiac’s case, the excess GERS funding would be enough to pay down the unfunded OPEBs and still leave money left over, according to Sobota’s estimates. It could be done as part of a negotiated agreement with the retiree plaintiffs. The problem is that city council would need to pass an ordinance and adopt standard MERS resolutions relinquishing control over GERS.

“We have discussed it,” said City Council President Pro Tem Mary Pietila. “We absolutely, adamantly, will not vote to take our GERS, which is in an overage… and give it to MERS.”

Other city council members did not return calls. Right now, GERS is all that the city has exclusive control over, Sobota said. Because it was overfunded, the emergency management law did not allow Schimmel to take over its operations. Pontiac's mayor, finance director and one city council member sit on the GERS board.

"This is more emotion over logic," Sobota said. "Logic says that if they want to get out from state receivership they need to give up something."