PROPOSED MEETING SCHEDULE AND WORK PLAN FOR THE STATE ADMINISTRATION AND VETERANS' AFFAIRS INTERIM COMMITTEE

Prepared for
The State Administration and Veterans' Affairs Interim Committee
by David D. Bohyer, Research Director

June 2005

Published By

Legislative Services Division

Part I: Proposed Meeting Schedule and Work Plan for the State Administration and Veterans' Affairs Interim Committee

INTRODUCTION

The State Administration and Veterans' Affairs Interim Committee (hereafter SAVA or Committee) is one of eight interim committee codified in Title 5, chapter 5, MCA.

> **5-5-228. State administration and veterans' affairs interim committee.** The state administration and veterans' affairs interim committee has administrative rule review, draft legislation review, program evaluation, and monitoring functions for the public employee retirement plans and for the following executive branch agencies and the entities attached to the agencies for administrative purposes:
> (1) department of administration;
> (2) department of military affairs; and
> (3) office of the secretary of state.

As one of the interim committees, the SAVA has various duties, responsibilities, and authority prescribed by statute, specifically, 5-5-215, MCA.[1]

> **5-5-215. Duties of interim committees.** (1) Each interim committee shall:
> (a) review administrative rules within its jurisdiction;
> (b) subject to 5-5-217(3), conduct interim studies as assigned;
> (c) monitor the operation of assigned executive branch agencies with specific attention to the following:
> (i) identification of issues likely to require future legislative attention;
> (ii) opportunities to improve existing law through the analysis of problems experienced with the application of the law by an agency; and
> (iii) experiences of the state's citizens with the operation of an agency that may be amenable to improvement through legislative action;
> (d) review proposed legislation of assigned agencies or entities as provided in the joint legislative rules; and

[1] Section 5-5-202, MCA, also speaks to the duties and authority of interim committees, as do other sections of Title 5, chapter 5, MCA.

(e) accumulate, compile, analyze, and furnish information bearing upon its assignment and relevant to existing or prospective legislation as it determines, on its own initiative, to be pertinent to the adequate completion of its work.

(2) Each interim committee shall prepare bills and resolutions that, in its opinion, the welfare of the state may require for presentation to the next regular session of the legislature.

(3) The legislative services division shall keep accurate records of the activities and proceedings of each interim committee.

The HB 2 appropriation and the budget allocated to the Committee may allow for approximately six or seven meetings. The precise number and duration of the meetings depends on a variety of factors, some of which have yet to be determined.

Pursuant to 5-5-217 and 5-11-105, MCA, the Legislative Council has assigned to the SAVA the study requested in House Joint Resolution No. 42, i.e., a study of state employee retirement plans. House Joint Resolution No. 42 was the top-ranked study as determined by the legislator poll conducted following adjournment sine die of the 59th Legislature. There has also been conjecture that the actuarial soundness of the state's retirement plans might be a subject of a potential special session in December 2005. Therefore, this proposed work plan and meeting schedule anticipates that the Committee will devote considerable attention to the HJR 42 study, particularly during the latter half of calendar 2005.

Thus, it is within the preceding context that this draft work plan and meeting schedule is proposed. The outline of a study plan for HJR 42 follows later in this proposal, as an integral part of the proposal, and as a self-contained outline.

WORK PLAN AND MEETING SCHEDULE

The Committee is more or less duty bound to execute its responsibilities as listed in Title 5, chapter 5, MCA. Consequently, staff anticipates that the agenda for each meeting of the Committee will include a component for agency updates, review of administrative rules, and public comment on issues within the purview of the Committee.

That said, however, for the first four meetings of the 2006-07 fiscal biennium, the draft work plan proposes that the Committee focus on the substance of HJR 42 and give only limited attention to other matters on an as-needed basis.

Beginning in 2006, the work plan and meeting schedule contemplate that the Committee will invest some energy in relevant issues beyond those contained in HJR 42, including state administration, purchasing/contracting, the National Guard and Reserves, veterans' affairs, elections, and political practices. By late-spring 2006, the Committee may wish to devote its attention to legislation contemplated by the agencies for which the Committee has review responsibilities and to consider concepts or proposals affecting any of the state's retirement plans.

In broad brush, staff proposes the following meeting schedule for the remainder of the 2005-06 interim.

- Friday, June 24, 2005
- Friday, September 2, 2005 (Friday before Labor Day?)
- Monday, October 3, 2005
- Friday, November 4, 2005
- Monday, December 2, 2005
- Friday, March 10, 2006
- Friday, May 12, 2006
- Monday & Tuesday, June 12 & 13, 2006
- Monday, September 11, 2006 (if necessary)

As suggested previously, the meetings in September, October, November, and December 2005 are anticipated to focus largely on state

retirement plan issues alluded to or specified in HJR 42. (More details on the anticipated HJR 42-focused meetings is provided later in this proposal.)

Beginning in March 2006, the Committee may wish to catch up with agencies' activities and emerging issues. By May 2006, the Committee should be reviewing legislation concepts or proposals related to any of the state's retirement plans from interest groups and the administration. Historically and traditionally, these issues have consumed substantial time and energy, both by the Committee and during regular legislative sessions.

By mid-June 2006, the agencies, for which the SAVA has been monitoring and reviewing responsibilities, should present legislation concepts and proposals other than those related to the state retirement plans under consideration for the 2007 legislative session for the Committee's review and action.

It is possible that the Committee could complete its work by the conclusion of the anticipated June meetings. However, it is equally as likely that the Committee may wish to tie up loose ends over the summer and conclude its work at a September 2006 meeting.

Importantly, the proposed meeting schedule and broad brush work plan is merely a proposal by staff. It is incumbent upon the SAVA members to revise the proposal as best suits the Committee, including the meeting dates, topics to be covered, and the like. Once adopted, the meeting schedule and work plan will guide staff work and the relevant activities of the agencies and interested parties attuned to the Committee's activities and schedule.

The proposed study plan for HJR 42, beginning on page 5, is an integral part of this proposed meeting schedule and work plan and, therefore, should also be revised and adopted in accordance with the Committee members' goals and objectives.

Part II: Proposed Study Outline for HJR 42 -- A Study of Public

Employee Retirement Plans

INTRODUCTION

Following a July 2004 biennial actuarial review of Montana public employee retirement plans, several of the public employee retirement boards identified an emerging problem that the boards felt deserved immediate and focused attention: the actuarial soundness of and funding for Montana's public employee retirement plans. More specifically, the biennial review revealed that three of the 10 retirement plans were significantly underfunded in actuarial terms. The boards determined that, under both Montana and federal law, there existed a pressing need for additional funding. Further, the boards determined that the law required that the additional funding be obtained through increased employer contributions to the plans.

As a result of the boards' determination, LC 96 and LC 100 were crafted and preintroduced as House Bills No. 148 and 181, respectively, for consideration by the 59th Legislature. In short, the bills would have, among other things, increased the employer contributions for covered employees in the Public Employees', the Sheriffs', the Game Wardens' and Peace Officers', and the Teachers' Retirement Systems.

While HB 148 and HB 181 were winding their way through the legislative process, mostly without controversy, the Governor's budget director, David Ewer, voiced his then-current concerns with the bills and the administration's desire to devote additional study and thought to the perceived predicament and to the options available to address it. Subsequently and relatively late in the session, HB 148 and HB 181 were tabled in the Senate Finance and Claims Committee.

Underlying the budget director's concerns and the Committee's action were the estimated multimillion dollar fiscal impacts for the current and future biennia, the potential for significant property tax increases at the local level to fund increased employer contributions, and the

possibility/probability that better solutions to the actuarial problems might be found by committing additional time and attention.

At about the same time that HB 148 began to meet resistance, House Joint Resolution No. 42 began its own venture into the legislative process. After receiving unanimous approval by the House State Administration Committee, HJR 42 successfully navigated through the House and the Senate in a scant 5 days.

BACKGROUND

The foundations of HB 148 and HB 181 and HJR 42 lie in the Montana Constitution, more precisely, in the provisions that speak to investing public retirement funds and to provisions that require actuarial funding of public pension systems.

> **Article VIII. Section 13. Investment of public funds and public retirement system and state compensation insurance fund assets.** (1) The legislature shall provide for a unified investment program for public funds and public retirement system and state compensation insurance fund assets and provide rules therefor, including supervision of investment of surplus funds of all counties, cities, towns, and other local governmental entities. *Each fund forming a part of the unified investment program shall be separately identified. Except as provided in subsections (3) and (4), no public funds shall be invested in private corporate capital stock. The investment program shall be audited at least annually and a report thereof submitted to the governor and legislature.*
>
> (2) The public school fund and the permanent funds of the Montana university system and all other state institutions of learning shall be safely and conservatively invested in:
>
> (a) Public securities of the state, its subdivisions, local government units, and districts within the state, or
>
> (b) Bonds of the United States or other securities fully guaranteed as to principal and interest by the United States, or

(c) Such other safe investments bearing a fixed rate of interest as may be provided by law.

(3) Investment of public retirement system assets shall be managed in a fiduciary capacity in the same manner that a prudent expert acting in a fiduciary capacity and familiar with the circumstances would use in the conduct of an enterprise of a similar character with similar aims. Public retirement system assets may be invested in private corporate capital stock.

(4) Investment of state compensation insurance fund assets shall be managed in a fiduciary capacity in the same manner that a prudent expert acting in a fiduciary capacity and familiar with the circumstances would use in the conduct of a private insurance organization. State compensation insurance fund assets may be invested in private corporate capital stock. However, the stock investments shall not exceed 25 percent of the book value of the state compensation insurance fund's total invested assets. (*Emphasis added in subsections (1) and (3).*)

Article VIII. Section 15. Public retirement system assets. (1) Public retirement systems shall be funded on an actuarially sound basis. Public retirement system assets, including income and actuarially required contributions, shall not be encumbered, diverted, reduced, or terminated and shall be held in trust to provide benefits to participants and their beneficiaries and to defray administrative expenses.

(2) The governing boards of public retirement systems shall administer the system, including actuarial determinations, as fiduciaries of system participants and their beneficiaries. (Emphasis added.)

The entirety of Article VIII, Section 15, and the relevant provisions of Art. VIII, Sec. 13, were voted on by the electorate in 1994 (Const. Amend. No. 25). Proponents of the provisions cited five reasons to support the measure:[2]

- prohibits the use of current public pension assets or future pension

[2] *1994 Voter Information Pamphlet*, Secretary of State, Arguments For Constitutional Amendment No. 25.

revenues for purposes unrelated to pension administration or benefit distribution (a.k.a. "pension raiding");
- requires the governing boards of our public pension systems to administer the systems and manage fund assets as "fiduciaries";
- maintains the effective day-to-day investment authority of the Montana Board of Investments;
- does not expand or provide any new benefit to public employees or retirees; and
- stabilizes the tax burdens expected of the public-at-large, as well as government employers and employees making payroll deduction contributions to the retirement funds.

The opponents cited a concern that CA 25 was tantamount to an admission that "the State is too insecure to pay back borrowed money from a fund or any other source" and, further, that the underlying message being sent "to all bond investors and others [is] that we are worried about the fiscal conditions of the State."as reasons to oppose it.[3]

The proponents carried the day as Constitutional Amendment No. 25 passed relatively easily, 243,855 or 73% in favor to 88,336 or 27% opposed.

STUDY ISSUES

The reasons for and concerns underlying HJR 42, as contained in the "whereas" clauses, include:
- the significant decline between 2000 and 2004 in the market value of public retirement plan investments that has resulted in actuarial losses to the public retirement plans totaling more than $1.3 billion;
- the fact that, using current assumptions, amortizing the liabilities in

[3] *1994 Voter Information Pamphlet*, Secretary of State, Arguments Against Constitutional Amendment No. 25.

the Teachers', Public Employees', Sheriffs', and Game Wardens' and Peace Officers' Retirement Systems will extended beyond 30 years;

- the constitutional requirement for actuarially-sound funding of the retirement systems, traditionally interpreted to mean a maximum 30-year amortization of liabilities;
- the specter of potential increases in public employer contributions to the under-funded retirement plans which would impact the state general fund and local governments' and schools' budgets;
- the estimate that the proposed increase in public employer contribution rates would require local governments and school districts to contribute an additional $20 million during the 2006-07 fiscal biennium, to be paid primarily through property taxes; and
- the responsibility of the Legislature to monitor and exercise a degree of oversight of the public employee retirement plans compelling legislators to consider how investment strategies, retirement benefits, and legislative policy decisions interact to affect employer funding obligations.

DIRECTION FROM THE LEGISLATURE

General directions to the Committee for conducting the study are contained in the "resolved" clauses of HJR 42. Those directions include:

- review constitutional and statutory language governing how public employee retirement plan funds are managed and invested;
- study the investment strategies, objectives, and asset allocation of public employee retirement funds managed by the Board of Investments;
- compare the asset allocation, investment performance, and actuarial assumptions regarding Montana's public employee retirement plan funds with asset allocation, investment performance, and actuarial assumptions used in other states;

- study how investments or asset allocation strategies are adjusted by the Board of Investments either in anticipation of changing needs or changing market conditions or after significant national and world events affect the market;
- study actual rates of return versus actuarial gains and losses in market value and how actuarially assumed rates of return adopted by the retirement boards relate to realized returns and the investment objectives set by the Board of Investments;
- examine how investments, retirement benefits, and legislative policy decisions interact to affect the actuarial soundness of the public employee retirement plans and employer funding obligations; and
- identify legislative policy issues and concerns, consider options, and develop recommendations.

Additionally, the Legislature commented that the SAVA explore whether technical assistance is available and can be provided to assist in conducting this study. The resolution suggests that, if considered to be appropriate by the SAVA, the Committee also receive staff assistance from the Legislative Fiscal Division and the Legislative Audit Division. Therefore, the SAVA members should consider what role, if any, the staffs of the Legislative Fiscal or Audit Divisions might fulfill.

PROPOSED STUDY DESIGN

The HJR 42 study can be approached in four phases that are, simultaneously, distinct and overlapping. As envisioned, the four study phases are:

I. building a foundation of facts and evidence regarding public employee retirement plans;
II. identifying and analyzing specific factors believed by the Committee to be influencing the fiscal/actuarial soundness of public employee retirement plans;

III. developing, through Committee discussion and action, findings and conclusions about:
   A. the actuarial conditions of the several public employee retirement plans; and
   B. the likely reasons for the respective conditions of the respective plans; and

IV. identifying, through Committee discussion and action, legislative options for addressing the fiscal/actuarial soundness of public employee retirement plans in Montana.

Phase 1: Building a foundation

Compiling facts and evidence about retirement plans will be ongoing throughout the study, but will largely be "front loaded". This phase of the proposed study design includes the following elements:

- a legal history of retirement plans in Montana. Staff will begin the historical review at the statutory implementation date of each of the retirement plans and provide an overview of constitutional and statutory requirements, restrictions, authority, etc. The implications of relevant case law decided subsequent to adoption of the Montana Constitution in 1972 will also be examined and interpreted.
- a literature review, conducted largely by staff and supplemented through research conducted independently by Committee members. The staff will develop and present a summary of the literature, plus some Montana-specific information on retirement plan issues.
- the experience and concerns of retirement plan stakeholders, i.e., representatives or groups potentially affected by the condition of public employee retirement plans, plus others considered by the Committee or staff to be directly impacted by the condition of public employee retirement plans.

Phase 2: Narrowing the focus

The scope of the HJR 42 study request is fairly broad. The proposed study plan provides an opportunity for the Committee to more clearly identify its own priorities within the guidelines provided in HJR 42. Subsequent to clarifying the Committee's priorities, the Committee members can articulate their individual concerns, questions, hypotheses, and so forth, about the ways in which various factors affect or cause changes in the fiscal/actuarial condition of retirement plans. This phase of the study will include:

- an issues and options decision tool, prepared by staff, that the Committee can use to clarify priorities and narrow the focus of the study. The objective of this exercise is to establish in relatively clear terms categories of or specific questions about public employee retirement systems, including: retirement plan investment theory; retirement plan practices in Montana and in other, selected states; factors and assumptions that affect the soundness of retirement plans; underlying causes of changes in the actuarial condition of public employee retirement plans in Montana;
- compiling or analyzing additional information, including information identified as necessary or useful to the Committee's future discussions or goals. The information may be provided by the "stakeholders" or the Committee's staff, or it may involve provoking more dynamic interaction between the Committee and others, such as a panel of experts or through topic-specific seminars conducted by experts.

Phase 3: Findings and conclusions

The questions and concerns identified, refined, and prioritized by the Committee in Phase 2 will provide the basis for continuing research and analysis. Subsequently, the accumulation of information and understanding by the Committee members will promote the development of findings from which the Committee can draw conclusions. This phase of the study will include:

- compiling, analyzing, and reporting information directly related to

the questions, concerns, and hypotheses developed previously by the Committee. This type of information may be available from current resources or it may have to be developed by staff, stakeholders, or Committee members. The Committee will establish formal findings by examining and discussing the information. (Decision tools can be developed by staff to assist in this exercise.)

- drawing conclusions from the findings adopted previously. The conclusions drawn through this exercise can form the basis for options, including proposed legislation, that may be developed in Phase 4.

Phase 4: Legislative options

The findings and conclusions developed in Phase 3 may lead the Committee to develop options for legislative consideration. In fact, that is the guidance provided in HJR 42. The options should be carefully crafted to address the legislatively-controllable factors and inputs relevant to public employee retirement plans in Montana.

For example, the Committee could propose that the 60th Legislature[4] adopt legislation to require, restrict, or initially authorize action by the Public Employee Retirement Board or its staff or the Board of Investments or its staff or expand the statutory authority already provided to either of the Boards or their respective staffs.

PROPOSED COMMITTEE MEETING SCHEDULE AND WORK PLAN

HJR 42 requires the study to be completed prior to September 15, 2006. Circumstances suggest, however, that there is some urgency to complete the study earlier, particularly when resolving retirement plan issues is a subject liable to be included in a likely special session

[4] The Committee might also prepare legislation for a special session, if one is called.

occurring this calendar year.

In broad terms, the Committee's budget will allow for about seven meetings, fewer if the meetings are 2-day ventures. A good portion of the Committee's first meeting will be devoted to organizational matters, including introductions to and overviews provided by the respective staffs of the agencies for which the SAVA has monitoring responsibilities. Depending on the nature and scope of issues other than HJR 42 that the Committee may address, the Committee may wish to devote at least 1/2 day of each meeting to HJR 42 and, if resolution of retirement funding is a special session topic, perhaps even an entire day of each meeting until after the special session, if one is called.

Based on a variety of factors, the proposed meeting dates for the Committee to engage in HJR 42-related activities are:

- Monday, June 27, 2005
- Friday, September 2, 2005 (this is the Friday before Labor Day?)
- Monday, October 3, 2005
- Friday, November 4, 2005
- Monday, December 2, 2005.

Following are preliminary outlines of tentative HJR 42-related items for each of the proposed meetings.

Friday, September 2, 2005

- Staff briefing on the legal history of public employee retirement plans in Montana.
- Briefings on retirement plan funding issues as perceived by PERB/PERA, TRB/TRS staff, BOI staff, et al.
- Briefing on the purpose, authority, and effect of the PERB/PERA, TRB/TRS staff, and BOI/BOI staff in regard to investing and managing funds held by the public employee retirement systems.
- Staff briefing on measures adopted by other states to address public employee retirement system funding issues.
- Committee work session to identify core areas of interest and

concern and narrow the focus of the study; develop hypotheses about cause and effect relationships between:

- ✓ public policies and actions taken by relevant boards and the respective boards' staffs to implement or achieve the policies;
- ✓ legislative action/inaction and the fiscal/actuarial status of public employee retirement systems;
- ✓ action/inaction of the respective boards and the fiscal/actuarial status of public employee retirement systems;
- ✓ action/inaction of the respective boards' staffs and the fiscal/actuarial status of public employee retirement systems;

- Direct additional research and analysis.

Monday, October 3, 2005

- Briefings on information related to hypotheses about state retirement plan and investment goals, objectives, and performance.
- Develop preliminary findings and conclusions.
- Direct additional research and analysis.

Friday, November 4, 2005

- Briefing on additional information related to questions and hypotheses about public employee retirement plans.
- Refinement of findings and conclusions previously developed.
- Develop additional or final findings and conclusions.
- Contingently or finally adopt findings and conclusions, as practical.
- Identify potential options to address retirement plan problems.
- Direct additional research and analysis.

Monday, December 2, 2005.

- Briefing on additional information, research, analysis.
- Adopt final findings and conclusions.
- Discuss options previously identified.
- Propose and discuss additional options.
- Contingently or finally recommend options for legislative

draft

consideration.

- Review, revise, and adopt proposed outline of Committee report to the Legislature.

If the Committee is unable to conclude its work at the December 2, 2005 meeting, completion and closure might be accomplished through a conference call or an additional meeting prior to the convening of the special session, if there is one.

SJR42/study outline 1.wpd
Cl0425 5171dbpa.

draft