

**HB 659: Study public retirement systems and redesign  
Teachers' Retirement System  
Draft Study Plan**

Prepared by  
Rachel Weiss, Research Analyst  
Legislative Services Division  
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**INTRODUCTION**

The issues surrounding retirement plans for state employees and teachers are rarely off the radar screen of the State Administration and Veterans' Affairs Committee (SAVA). Whether SAVA is studying an overhaul of the system or just tweaks here and there, retirement plans always generate questions and legislation.

In many ways, HB 659 is a continuation of the work done by SAVA during the late 1990s and the 2005-06 and 2007-08 interims. A resolution introduced in the 2007 Legislature -- HJR 59 -- required the Committee to conduct an in-depth study of the state's retirement plans, principles and guidelines for retirement policies in general, and best practices for retirement plans. The result was a wealth of information on retirement plans and funding methods, including an update to a comprehensive manual for legislators and others about Montana's statewide retirement systems. Much of SAVA's work this interim on HB 659 will be based on information and analysis generated for the HJR 59 study.

**CONSTITUTIONAL REQUIREMENTS**

The Montana Constitution addresses the public retirement systems directly in two sections in Article VIII.

Section 13 allows public retirement system fund assets to be invested:

**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.

**History: Amd. Const. Amend. No. 25, approved Nov. 8, 1994; amd. Const. Amend. No. 34, approved Nov. 7, 2000.**

Section 15 requires the public retirement systems to be funded on an actuarially sound basis and puts limits on what can be done with retirement system assets. It also requires the governing boards of the systems to manage the assets as "fiduciaries".

**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.

**History: En. Sec. 2, Const. Amend. No. 25, approved Nov. 8, 1994.**

## STUDY BACKGROUND

HB 659 gives SAVA a broad mandate: examine and recommend changes to the statewide retirement systems, including a redesign of the Teachers' Retirement System (TRS). However, the "whereas" clauses of the bill give insight into the reasons for the study and include:

- ! that the Montana Constitution requires the retirement systems to be funded on an actuarially sound basis;
- ! the current economic downturn adversely affected the market value of investments and, thus, the funding status of the retirement systems;
- ! the most recent actuarial valuation for TRS showed that with the then-current actuarial assets and liabilities, the current contribution rates will not amortize the system's unfunded liability within the benchmark 30-year

- period;
- ! if investment earnings continue to decline the TRS liabilities will not amortize in any length of time unless significant funding is provided to the system and the system is redesigned; and
- ! actuarial projections that include market declines after July 1, 2008, may show that the retirement systems administered by the Public Employees' Retirement Board may not amortize in any length of time without increased contributions and benefit changes or plan design changes.

The resolution also provides that SAVA should look at the funding and benefits for all the retirement programs in light of their place in the overall compensation package received by a public employee and develop legislation for consideration by the 62nd Legislature.

#### DIRECTION FROM THE LEGISLATURE

The State Administration and Veterans' Affairs interim committee is already charged by Section 5-5-228(2)(a), MCA, to "consider the actuarial and fiscal soundness of the state's public employee retirement systems," and to "study and evaluate the equity and benefit structure" of those systems. More specifically, HB 659 requires SAVA to:

1. review current trends and best practices in public retirement plan design and funding; and
2. examine options for changes to each of the retirement systems administered by the Public Employees' Retirement Board.

The changes SAVA should consider for these 10 funds include, but are not limited to, changes in the benefit formula multiplier for each year of service and the minimum age at which a member is eligible for full retirement benefits or reduced, early retirement benefits.

For TRS, the Legislative mandate is much more specific: the committee must "compare and contrast" options for redesigning the system and develop legislation to implement that redesign. The bill also provides that any redesign of TRS *must*:

1. ensure members will have a guaranteed benefit in retirement;
2. provide that employers and employees share the risk of actuarial gains and losses and allow for adjustment of contributions to meet that requirement;
3. be sustainable and funded on an actuarially sound basis;
4. provide benefits designed to attract qualified and competent employees;
5. comply with the Internal Revenue Code governing tax-qualified public pension plans;
6. keep the Teachers' Retirement Board as the administrator of the system and the Board of Investments as the investor of the plan's assets; and
7. provide a foundation for financial security.

The bill provides a bit of clarification for the meaning of "foundation" by stating:

1. a retirement plan is only one part of an employee's total compensation;
2. the employer-sponsored plan is not intended to be the sole provider of income to an individual in retirement; and
3. deferred compensation, personal savings and investments, and Social Security should also play some role in a person's retirement income plans.

SAVA is also authorized to contract for consulting services, but the type of service and the extent to which the Committee chooses to use that service is up to the members to decide. The 61st Legislature made resources available to support the HB 659 study in the form of a \$200,000 appropriation.

### GENERAL STUDY DESIGN

Although the direction the study takes ultimately depends on choices the Committee will make in its first few meetings, it is possible to lay out five general study phases and estimate the amount of time that should be devoted to each phase.

- I. Review of existing plans and assessment of committee's desire for more background information (pre-meeting and additional time as requested)
- II. Initial study design choices -- overview and decision-making (1-2 meetings)
- III. Develop and analyze options for plan changes or redesigns (2-3 meetings)
- IV. Select options to recommend (1 meeting)
- V. Refine and finalize recommendations (2 meetings)

#### **Phase I: Review and assessment**

Because the Committee must make important choices relatively early in the process about how it wishes to proceed, the first phase will largely be conducted before any formal meetings are convened. Staff will send each Committee member *A Legislator's Guide to Montana's Public Retirement Systems: 2008*, along with several general questions to start the process of thinking about retirement plans in general and each legislator's philosophies about the role and structure of retirement plans in Montana's employee compensation package. Staff will also complete follow-up calls to each member to ascertain if there is additional information that the member might like to receive or have researched. Each Committee member will receive key documents and analysis generated by the 2007-08 SAVA Committee's study of public employee retirement systems. Depending on the members' wishes, it is possible to devote part of another meeting to furthering their knowledge of Montana's various public employee retirement systems and the investment of the assets of those systems.

#### **Phase II: Initial study design choices**

Because of the complexity of the task before the Committee, the need for actuarial analysis of any redesign or plan changes proposed by the Committee, and the \$200,000 appropriation to the study, SAVA members will have to make some key

decisions about how they wish to structure their study process and if they want to contract for outside consulting assistance.

To assist Committee members in understanding the variety of options available to them, the organizational meeting will allow stakeholders of HB 659 time to testify briefly on the bill and voice their recommendations about conducting the study. Committee members can then make decisions based on what they think is best. Because of the extensive requirements of the HB 659 study and the finite resources of Committee member and staff time, the Committee will need to make several decisions at its first meeting or its second at the latest.

Also, because the Committee will need to have an actuary evaluate any plan redesigns or changes, members should allow themselves time to develop and analyze options before early spring 2010 in order to give the actuary time to review proposals. This recommended deadline means the committee cannot procrastinate too long in the decision-making process if it wishes to complete its task.

A list of options will be presented later in Appendix A on page 9, but might include such things as:

- contracting with a plan design consultant to lead the Committee through the process;
- contracting with an actuary;
- using the actuaries already under contract with the Public Employees' Retirement System and the Teachers' Retirement System, if possible; or
- forming a subcommittee.

### **Phase III: Identify and analyze options**

When Committee members are comfortable with their knowledge of public employee retirement plans, have made documented findings and conclusions, and have decided how to proceed, they will want to investigate and develop potential changes to the retirement systems, including options to redesign the TRS within the boundaries set out by HB659. Members may use information suggested to them by the various stakeholders or experts in the retirement planning field, as well as members' own knowledge and public input.

During this stage, the Committee will also want to review and adopt principles and guidelines to use in comparing and evaluating the various redesign and plan change options before them. The current principles adopted by the 2007-08 SAVA can be found on page 71 of *A Legislator's Guide to Montana's Public Retirement Systems: 2008*. The Committee may choose to modify, replace, or keep those principles, but will need something in place against which it can compare its work.

### **Phase IV: Select options to recommend**

After completing Phase III, the Committee may wish to develop certain options for

legislative consideration. HB 659 requires the Committee to consider changes to the public retirement systems in general and to offer a redesign of the TRS. Having selected the options it wishes to pursue by using the principles it has reviewed and adopted in Phase III, the Committee should forward to an actuary any proposed changes that the members would like to have reviewed and analyzed. This process will give the Committee further information to be used in the final decision-making process that is Phase V.

### **Phase V: Revise, finalize, and adopt recommendations**

With the actuarial analysis of potential plan design changes complete, Committee members will have the necessary information to revise their earlier recommendations and construct and adopt final recommendations, which might include legislation, for the 62nd Legislature.

If the Committee decides that it will take no action, it should consider making a clear statement to that effect and supporting this statement with findings and conclusions developed as a result of the earlier phases of the study.

If the Committee wishes to forward legislation on to the 62nd Legislature for consideration, it will need to approve draft language and should agree upon a bill sponsor. The legislation, and indeed the Committee's work in general, will need to be complete by the September 15, 2010, deadline, and any legislation will need to be pre-introduced.

### **PROPOSED COMMITTEE MEETING SCHEDULE AND WORK PLAN**

Although this study plan does not anticipate the formation of a subcommittee to study HB 659, this suggested schedule can be adjusted to allow for a subcommittee to meet in conjunction with each full Committee meeting.

The following are preliminary outlines of the tentative HB659-related items for each of the proposed meetings in the work plan:

#### *Friday, June 26, 2009*

- ▶ General overview of the requirements of the HB 659 study
- ▶ Stakeholder presentations of priorities and decision points they wish the Committee to consider
- ▶ Committee action on certain decisions if wished

#### *Friday, September 25, 2009*

- ▶ Responses to Committee requests from previous meeting(s)
- ▶ Committee action on any remaining decisions left from organizational meeting
- ▶ Briefing on the *Principles and Guidelines for Public Employee Retirement Systems*

- ▶ Briefing on existing retirement plan benefits and drawbacks as perceived by various stakeholders
- ▶ Committee discussion to identify areas of interest and concern
- ▶ Committee discussion and/or agency or stakeholder presentations to generate potential options for policy changes and TRS redesign

*Friday, October 30, 2009*

- ▶ Responses to Committee requests from previous meeting(s)
- ▶ Committee discussion on and revision and adoption of Principles and Guidelines to guide the 2009-2010 SAVA and the 62nd Legislature
- ▶ Refinement of options identified in previous meeting
- ▶ Propose and discuss additional options

*Friday, December 11, 2009*

- ▶ Responses to Committee requests from previous meeting(s)
- ▶ Refine options identified and discussed in previous meetings
- ▶ Further presentations from experts and stakeholders as requested and necessary
- ▶ Begin to develop findings and conclusions

*Friday, January 22, 2010*

- ▶ Responses to Committee requests from previous meeting(s)
- ▶ Refine and discuss previous findings and conclusions for plan redesign or change
- ▶ Develop or adopt new or additional finding and conclusions
- ▶ Direct additional research and analysis or draft legislation
- ▶ Identify initial recommendations

*Friday, March 5, 2010*

- ▶ Responses to Committee requests from previous meeting(s)
- ▶ Committee discussion and action to determine which options and recommendations for plan redesign and/or change to adopt and forward to an actuary for review and analysis

*Thursday/Friday, April 22-23, 2010*

- ▶ Responses to Committee requests from previous meeting(s)
- ▶ Consider initial response from actuary
- ▶ Refine, review, reject or adopt previous recommendations for plan redesign or change
- ▶ Review any initial draft legislation proposed by the Committee as a result of HB 659 for the 62nd Legislature
- ▶ Forward any new recommendations or options to actuary for review
- ▶ Forward any design changes to a tax counsel for review, if necessary

*Thursday/Friday, June 24-25, 2010*

- ▶ Responses to Committee requests from previous meeting(s)
- ▶ Consider responses from actuary and tax counsel
- ▶ Adopt final findings, conclusions, and recommendations including draft legislation

\*\* This work plan is a *draft*, subject to review and change by the Committee. It might face alteration depending on choices made by the Committee about consultants, actuaries, and subcommittees. If the Committee chooses to issue an RFP for a consultant or actuary or both, staff anticipates needing to have the RFP approved during the summer or early fall of 2009, either by conference call or at the September 2009 meeting in order to keep the Committee on track to develop and send potential legislation for actuarial review by the end of March 2010.

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## Appendix A: House Bill 659 Study Decision Points

| Decision Point  | Pros/Cons   | Decision |
|---|---|----------|
| <p>Contract with an actuary</p>   | <p><b>Pros</b></p> <ul style="list-style-type: none"> <li>• Committee gets dedicated, possibly more independent, actuary to provide analysis of redesign and any suggested changes</li> <li>• Analysis will be required for any legislation resulting from the committee's study</li> <li>• Other?</li> </ul> <p><b>Cons</b></p> <ul style="list-style-type: none"> <li>• Might require lengthy RFP and selection process</li> <li>• Could be expensive</li> <li>• Actuary might have to catch up quickly on Montana's plan designs and database structure</li> <li>• Other?</li> </ul> |          |
| <p>Use existing actuaries for TRS and PERS and reimburse for services</p> | <p><b>Pros</b></p> <ul style="list-style-type: none"> <li>• Takes advantage of existing relationships and expertise</li> <li>• Possibly less expensive than hiring independent Committee actuary</li> <li>• Would avoid lengthy RFP process</li> <li>• Other?</li> </ul> <p><b>Cons</b></p> <ul style="list-style-type: none"> <li>• Potential conflict of interest for current actuaries</li> <li>• Other?</li> </ul>  |          |

| Decision Point  | Pros/Cons  | Decision |
|---|--|----------|
| <p>Contract with plan design consultant (who might also be an actuary) to lead the Committee in the study</p> | <p><b>Pros</b></p> <ul style="list-style-type: none"> <li>• Would provide outside expertise and perspective</li> <li>• Might present different range of options than committee would otherwise develop on its own</li> <li>• Depending on the RFP and consultant, might be able to combine research and actuarial evaluation phases</li> <li>• Might be able to provide assistance with the tax requirements of any new proposal</li> <li>• Other?</li> </ul> <p><b>Cons</b></p> <ul style="list-style-type: none"> <li>• Delay of developing and issuing RFP might put SAVA in a time crunch</li> <li>• Interim time line might not provide enough time for a consultant to evaluate and present options</li> <li>• Other?</li> </ul> |          |

| Decision Point       | Pros/Cons  | Decision |
|----------------------|--|----------|
| Appoint subcommittee | <p><b>Pros</b></p> <ul style="list-style-type: none"> <li>• Full committee could devote time to other SAVA issues</li> <li>• Could delegate hiring of actuary and/or consultant to subcommittee</li> <li>• Other?</li> </ul> <p><b>Cons</b></p> <ul style="list-style-type: none"> <li>• Full committee must ultimately approve any recommended plan changes or redesigns, resulting in duplication of effort</li> <li>• Members not on subcommittee will have less information on the plans yet still have to make decisions on final recommendations</li> <li>• Extra meetings will use budget that could be used for hiring consultant/actuary</li> <li>• Subcommittees tend to work best with a narrow, well-defined delegated task, not with a broad grant of authority</li> <li>• Staff, secretarial and member time is limited</li> <li>• Other?</li> </ul> |          |

| Decision Point         | Pros/Cons  | Decision |
|------------------------|--|----------|
| Adopt HB659 study plan | <p><b>Pros</b></p> <ul style="list-style-type: none"> <li>• Outlines work for next 12-15 months</li> <li>• Is flexible and can be adjusted if necessary</li> </ul> <p><b>Cons</b></p> <ul style="list-style-type: none"> <li>• Might not address Committee members' wishes, needs, or concerns</li> <li>• Commits Committee to a general plan of action</li> </ul> |          |
| Others?                |  |          |