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State Administration and Veterans' Affairs Interim Committee

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DRAFT FINAL REPORT TO THE 68TH MONTANA LEGISLATURE

DRAFT 2022 LEGISLATOR'S GUIDE TO MONTANA'S PUBLIC EMPLOYEE RETIREMENT SYSTEMS & HJ 8 FINAL REPORT

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This report is a summary of the work of the State Administration and Veterans' Affairs Interim Committee, specific to the SAVA Interim Committee's 2021-2022 pension study as outlined in the SAVA Interim Committee's 2021-22 work plan and House Joint Resolution 8 (2021). Members received additional information and public testimony on the subject, and this report is an effort to highlight key information and the processes followed by the SAVA Interim Committee in reaching its conclusions. To review additional information, including audio minutes, and exhibits, visit the SAVA Interim Committee website: https://leg.mt.gov/committees/interim/sava/.

A full report, including links to the documents referenced in this print report, is available at the SAVA HJ 8 study page: https://leg.mt.gov/committees/interim/sava/hj-8/.

INTRODUCTION

Overview

The 2022 Legislator's Guide to Montana's Public Employee Retirement Systems is intended to serve as a tool for legislators to use when examining Montana's public employee retirement systems and related policy issues. The State Administration and Veterans' Affairs Interim Committee (SAVA) has been producing the Legislator's Guide since 2008 to provide background information, reference material, and context for legislators as they make decisions related to the state's retirement systems. This year, the Guide also includes a chapter on the HJ 8 interim study on pensions conducted by the SAVA committee during the 2021-2022 interim.

Impact to Montana

As of June 30, 2022, the actuarial value of trust fund assets in Montana's nine defined benefit public employee retirement systems totaled more than $13.8 billion. The actuarially accrued liability (AAL) totaled more than $18.6 billion, of which over $4.7 billion is considered unfunded (UAAL).

There are currently 55,075 active members enrolled and 47,196 retirees and benefit recipients – roughly 9% of the state's population or 1 out of every 11 Montanans. There are over 1,200 employers across the state, including local governments, school districts, community colleges, and state agencies.

Role of the SAVA Interim Committee

Under section 5-5-228, Montana Code Annotated, the SAVA committee shall:

a. consider the actuarial and fiscal soundness of the state's public employee retirement systems, based on reports from the teachers' retirement board, the public employees' retirement board, and the board of investments, and study and evaluate the equity and benefit structure of the state's public employee retirement systems;
b. establish principles of sound fiscal and public policy as guidelines;
c. as necessary, develop legislation to keep the retirement systems consistent with sound policy principles; and
d. publish, for legislators' use, information on the public employee retirement systems that the committee considers will be valuable to legislators when considering retirement legislation.

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CHAPTER 1 – HJ 8 (2021)

Introduction

HJ 8, passed during the 2021 Legislative Session, calls for an interim study of Montana's defined benefit public employee retirement system and the development of a long-term strategic approach to funding the systems. Included in the resolution are the following tasks for the SAVA interim committee:

1) study the financial stability of Montana's defined benefit public employee retirement systems;
2) use the assistance of independent certified professional actuaries, if funding is made available by the Legislature for the actuarial services*;
3) investigate the actuarial impact on funded ratios and amortization schedules of alternative funding policies for determining required contributions and consider selected scenarios, recognizing the funding sources for and the relative health or weakness of these unique systems;
4) review and study the governance structure of the public employee retirement systems;
5) examine legislative education, oversight, and goals concerning the public employee retirement systems, including decision benchmarks or indicators for future action; and
6) develop recommendations for a long-term strategic approach to setting contribution rates that will ensure the financial strength and resilience of the retirement systems while recognizing the responsibility placed on the taxpayers and citizens of this state.

The following directions are also included in the study resolution:

- The SAVA Interim Committee invite two members of the Legislative Finance Committee, a Senate member, and a House of Representatives member, one from the majority party and one from the minority party, to participate with, but not be voting members of, the SAVA Interim Committee on matters related to this study.
- The Legislative Services Division provide research, legal, and administrative staff support for the SAVA Interim Committee and that the SAVA Interim Committee presiding officer may request that the Legislative Fiscal Division provide fiscal analysis as needed.
- The study be conducted, and the recommendations be developed, in consultation with all interested stakeholders, including but not limited to representatives of:
    - the state's taxpayers;
    - active and retired members of the retirement systems;
    - employers, including local governments, school districts, and state agencies;
    - key agencies, including the Governor's office, the retirement boards, and the Board of Investments; and
    - other interested parties as considered appropriate.
- All aspects of the study, including presentation and review requirements, be concluded prior to September 15, 2022.
- The final results of the study, including any findings, conclusions, comments, or recommendations, be reported to the 68th Legislature.

**funding was not made available for this component of the study*

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Topics by Meeting

The SAVA interim committee worked on the HJ 8 study at each of their meetings during the 2021-2022 interim. Here is a breakdown of topics presented and discussed at each meeting:

- The SAVA interim committee met for the first time of the 21-22 interim on **June 24, 2021**. During the meeting, staff introduced the study and the committee voted to set aside 70% of their time during the interim to the study.
- At the **August 25, 2021**, meeting committee members received Pensions 101 presentations from committee staff, and representatives from the Montana Public Employee Retirement Administration (MPERA), the Teachers' Retirement System (TRS), and the Montana Board of Investments (BOI), providing a high-level overview of the state's retirement systems. Committee members also heard from stakeholders, including union representatives, individual retirement system representatives, active members, and retirees about their suggested approaches to the study and the importance of the state's retirement systems.
- The **November 4, 2021**, presentations focused on the governance structure of the retirement systems and the system of oversight and checks and balances. Presenters included committee staff, representatives from MPERA, TRS, the Legislative Audit Division (LAD), and the Legislative Fiscal Division (LFD). Committee staff also shared data about other states' retirement plans and a draft version of the FY21 green sheets with the committee.
- The SAVA interim committee met the morning of **December 16, 2021**, to hear about the history and funding status of the Game Wardens' and Peace Officers' Retirement System (GWPORS) and to review the finalized FY21 green sheets. In the afternoon, the SAVA interim committee held a joint meeting with the Legislative Finance Committee (LFC) to hear the FY21 annual actuarial valuation reports from MPERA and TRS and discuss the results.
- The **March 24, 2022**, meeting included presentations about plan design and amortization policy from national experts from the National Association of State Retirement Administrators (NASRA), the National Institute on Retirement Security (NIRS), the National Conference on Public Employee Retirement Systems (NCPERS), and Cavanaugh Macdonald Consulting, LLC. In addition, the committee learned about the history of the Montana University System's Retirement Program (MUS-RP), its split from TRS in 1993, and the supplemental contribution from the MUS to TRS to pay off its remaining obligations.
- At the **May 25, 2022**, meeting committee members heard the results of the MPERA and TRS experience studies, which are conducted every four years by an actuary. The studies included comparisons of the actual experience of the individual retirement systems with the projections and suggested changes to several assumptions, including the rate of return and multiple demographic data points. In addition, committee staff presented on the history of general fund contributions to the retirement systems, including the Treasure State Endowment Program (TSEP) fund.
- The committee held a two-day meeting **August 10-11, 2022**. Committee staff shared a draft bill, prepared at the request of the committee, amending 19-3-316, MCA, extending the PERS-DB supplemental employer contribution to 2034 and increasing the rate by 1% gradually over ten years. Committee members approved the provisional draft and Representative McKamey offered to carry the bill. Committee staff presented the committee with an options paper in response to their request for supplemental funding for GWPORS and an adjustment to the GWPORS employer contribution rate. After some discussion, the committee members directed

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staff to draft a bill for review at their October 26 meeting giving one-time-only general fund contributions to the public safety retirement systems to help them amortize in 30 years or less and to amend 19-8-504, MCA, increasing the GWPORS employer contribution rate making it the same as the employee contribution rate. Committee members also directed staff to prepare two other bill drafts for their October meeting – a study resolution for the 2023-2024 interim that would focus specifically on PERS-DB and TRS working with the Legislative Finance Committee and a bill that would add a policy statement to statute stipulating that no new benefits can be added to an individual pension system unless they are fully funded. The committee voted to create a subcommittee – the Pensions Working Group – to craft the language for the policy statement. Representative Julie Dooling was appointed Chair of the subcommittee. The committee gave staff instructions on the HJ 8 final report.

- The Pensions Working Group met **September 6, 2022**, to develop language for the benefit policy statement. The subcommittee members agreed on the following language to be added to each pension system chapter in the MCA and directed staff to draft a bill for the entire committee's consideration in October:
    - "It is the policy of the state that additional benefits may not be added to the (system name) unless the system amortizes in 30 years or less and the additional benefit is fully funded in perpetuity."
- The final SAVA meeting is scheduled for **October 26, 2022** and the committee is scheduled to hear the FY22 actuarial valuation reports from MPERA and TRS, review the draft HJ 8 final report, review the FY 22 green sheets, and review draft committee legislation.

HJ 8 study presentations, briefing memos, and materials from each SAVA meeting can be found here: https://leg.mt.gov/committees/interim/sava/hj-8/.

Committee Findings

- There are nine statewide defined benefit retirement systems in Montana, covering 55,075 active employees and 47,196 retirees and benefit recipients. There are over 1,2000 employers across the state, including state agencies, local governments, and school districts.
- The actuarial value of the trust fund assets of the statewide defined benefit systems totals more than $13.8 billion.
- The actuarially accrued liability (AAL) for the systems totals more than $18.6 billion, of which over $4.7 billion is considered unfunded (UAAL).
- There are multiple systems that do not amortize in 30 years or less, as is required by the Montana Constitution and the MCA.

Committee Recommendations

- Add a policy statement to each individual pension system barring additional benefits unless the individual system amortizes in 30 years or less and the new benefit is fully funded in perpetuity.
- Conduct an additional pension study during the 2023-2024 interim in conjunction with the Legislative Finance Committee, looking specifically at PERS-DB and TRS as they are the largest retirement systems in the state, and focusing on funding models and possible funding policy changes.

- Extend the supplemental PERS-DB employer contribution until 2034 and increase the rate 1% gradually over the ten-year period.
- Provide one-time cash infusions from the general fund to the public safety systems that do not currently amortize in 30 years or less – the Sheriffs' Retirement System (SRS), the Game Wardens' and Peace Officers' Retirement System (GWPORS), and the Highway Patrol Officers' Retirement System (HPORS).
- Increase the GWPORS employer contribution rate to match the employee contribution rate.

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CHAPTER 2 – PRIMER ON RETIREMENT PLANS

Purpose of Retirement Plans

Retirement plans started as an alternate method for employers to compensate their employees for services rendered. Later, employers used retirement plans as a recruiting and retention tool that supplemented regular compensation. Today, employers often view retirement plans as a method to recruit, compensate, and retain employees. Employees typically view employer-sponsored retirement plans as their primary way to save and invest their earned compensation to ensure financial security in retirement.

Types of Retirement Plans

There are three major types of retirement plans in the public sector: defined benefit (DB), defined contribution (DC), and hybrid plans. There is no universal answer as to what is considered the optimal retirement plan structure, as this varies based on the needs and objectives of the plan sponsor and population covered, and the legal and regulatory environment of the state or municipality.

Defined Benefit Plans

- A defined benefit (DB) plan is an employer-sponsored retirement plan that provides a specific monthly benefit at retirement. The employee's salary and length of service determine the retirement benefit.
- DB plan funds typically include a combination of employer contributions, employee contributions, and investments earnings. Actuarial valuation results determine recommendations for contribution rates.
- Public pension assets are put into a pooled trust fund and are managed by professionals at the state level. The pooled trust fund assets are invested to pre-fund the cost of pension benefits, providing economies of scale that lower fees and increase returns. Retirees receive set monthly installments rather than a lump sum and the benefit is guaranteed for the rest of their life.
- Investment performance does not affect the value of a DB plan benefit but may affect or cap cost-of-living adjustments.
- The typical DB plan places some responsibility and risk on both the employer and employee.
- DB plans are the most prevalent plan design in the public sector.

Defined Contribution Plans

- A defined contribution (DC) plan is an employer-sponsored retirement savings vehicle that accumulates savings based on contributions to an employee's individual retirement account. DC plans do not promise a specific retirement benefit.
- In a DC plan, the employee, employer, or both contribute to the plan. The contribution amount is typically a certain percentage of the employee's salary.

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- DC plans typically do not pool assets, and instead, employees have a range of investment options to manage individually. The employee receives the balance in their account upon retirement. The 401(k) plan is the most popular form of DC plan.
- Employees assume the investment and longevity risks in DC plans. Employers fulfill their annual obligations as their contributions are made but may face some uncertainty about timely retirements if investment returns drop close to an employee's retirement date and the employee decides to delay.
- Many states offer employees a DC plan as a supplemental retirement savings plan or as an optional alternative to the DB plan. Three states – Alaska, Michigan, and Oklahoma – and the District of Columbia offer only a DC plan on a statewide basis for broad employee groups.

Hybrid Plans

- Hybrid pension plans combine elements of both DB and DC plans. The most common government-sponsored hybrid plan types are combination plans and cash balance plans.
- Combination plans feature a DB component that is typically more modest than a traditional DB plan combined with a mandatory DC plan. Eleven states offer combination hybrid plans, either optional or compulsory.
- Cash balance plans combine elements of traditional pensions with individual savings accounts into a single plan. Employers generally guarantee an annual rate of return on an account the employer, employee, or both contribute. Five states offer cash balance hybrid plans: California, Kansas, Kentucky, Nebraska, and Texas.
- Core elements of all hybrid plans include mandatory participation, shared financing and risk among employers and employees, pooled assets, and required lifetime benefit payouts.

Inherent Risks

There are different perspectives concerning the advantages and risks of DB, DC, and hybrid plans. Although the risks are the same with any plan, the plan's design dictates how risk is managed and the extent to which the employer and employee share the responsibility for managing the risks.

Any retirement plan will have to cope with the following risks:

- Investment risks and market volatility.
- Longevity risks, i.e., whether the benefit will last to the end of a retiree's life.
- Inflation risks, i.e., how to provide postretirement benefit increases to keep up with cost of living.

Also, DB, DC, and hybrid plans will offer different approaches about how to provide the following:

- Sufficient benefits in retirement.
- Flexibility.
- Portability.

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Public v. Private Retirement Plans

Private sector employers have switched from primarily offering DB plans to primarily offering DC plans, such as 401(k) plans. According to the U.S. Bureau of Labor Statistics, as of March 2020, 76% percent of state and local workers in the U.S. participated in defined benefit plans while 18% participated in defined contribution plans.

Supplemental Plans

Montana state government employees and some local government employees may also voluntarily participate in a 457(b) deferred compensation plan to help supplement their retirement plans. School districts and universities may establish 403(b) plans for their employees, and many Montana school districts, and the Montana University System have done so. An individual public employee may also establish a traditional IRA or Roth IRA. Contributions to a traditional IRA are tax deductible if the employee's income does not exceed a certain threshold.

Social Security

The 1935 Social Security Act did not originally allow state and local government employees to participate in Social Security. In 1950, the act was amended to make coverage optional for certain state and local government employees, but still left many public employee groups uncovered. The option for states to allow certain public employees to participate was expanded in subsequent amendments to the act. Congress made Social Security coverage mandatory, starting in July 1991, for most state and local government employees not already covered by a public pension plan. Coverage is provided to these employees through individual agreements with state and local governments.

Pension Regulation

Sections 400 through 419 of Title 26, U.S.C.—Title 26 is the Internal Revenue Code (IRC)—and attendant federal administrative regulations govern public and private pension plans. Qualified pension plans are plans that comply with the IRC and applicable provisions of the Employee Retirement Income Security Act of 1974 (ERISA). ERISA specifies nondiscrimination standards and regulates reporting and accounting procedures. Qualified plans receive favorable tax treatment; nonqualified plans do not. Except for certain administrative and accounting standards, ERISA does not apply to public pension plans. However, public plans must be qualified under various sections of the IRC in order for employee contributions and accruing benefits to be tax deferred.

GASB Financial Reporting

New Governmental Accounting Standards Board (GASB) reporting requirements under GASB Statement No. 67, Financial Reporting for Pension Plans, and GASB Statement No. 68, Accounting and Financial Reporting for Pensions, in 2015 changed how public employers in Montana who participate in a public employee retirement plan must calculate and report pension costs and obligations on their individual governmental financial statements.

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Under the new GASB statements, the employers who participate in cost-sharing multiple-employer retirement plans (such as Montana's statewide public employee retirement plans) are now required to show pension obligations on their individual financial statements rather than only on a combined financial statement.

The way that pension liabilities are calculated and shown under the new GASB requirements is different from the way actuaries calculate and show these liabilities for actuarial valuations. Because of these different calculations, the GASB reports may show a higher pension liability than the actuarially calculated liability and therefore also show a lower funded ratio for the plan.

Under GASB, the term "discount rate" is used when referring to the assumed rate of return on investments because the calculations involve discounting (or translating) the future value of assets and liabilities into present values. The discount rate used for the GASB report will be the same as the actuarial assumed rate of return used in the actuarial valuations as long as the assets are projected (under GASB calculations) to be sufficient to pay the future benefits.

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CHAPTER 3 – OVERVIEW OF MONTANA'S PUBLIC EMPLOYEE RETIREMENT SYSTEMS

Montana's Statewide Retirement Systems

Most of Montana's statewide public employee retirement systems originated as local government and school district plans. Over time, local jurisdictions opted to join the state's plans or to combine their local plans into one statewide plan. The first statewide system, the Teachers' Retirement Systems (TRS), was formed in 1937. The state's largest plan, the Public Employee Retirement System (PERS), was created in 1945 with the Public Employees Retirement Law. The most recent plan, the PERS Defined Contribution Plan (PERS-DC), was formed in 1999. There are now 11 public employee retirement systems in Montana – 9 DB plans and 2 DC plans. These systems cover nearly all state and local government employees and school district employees. In addition, many state employees are eligible to join the optional supplemental 457(b) Deferred Compensation Plan.

Creation of Montana's Statewide Public Employee Retirement Systems

- 1937 –Teachers' Retirement System (TRS) is established.
- 1945 – Public Employees Retirement Law is passed; Public Employees' Retirement System (PERS-DB) and Highway Patrol Officers' Retirement System (HPORS) are established.
- 1963 – Game Wardens' and Peace Officers' Retirement System (GWPORS) is established.
- 1965 – Volunteer Firefighters' Compensation Act (VFCA) is passed.
- 1967 – Judges' Retirement System (JRS) is established.
- 1974 – Municipal Police Officers' Retirement System (MPORS) and Sheriffs' Retirement System (SRS) are established.
- 1981 – Firefighters' Unified Retirement System (FURS) is established.
- 1987 – Montana University System Retirement Program (MUS-RP) is established.
- 1999 – PERS Defined Contribution Retirement Program (PERS-DC) is created.

Governing Boards

Each plan's governing board members are the plan's responsible fiduciaries, meaning they must act only in the best interest of plan members and their beneficiaries. Nine of Montana's retirement plans (8 DB & 1 DC) are governed by the Public Employees' Retirement Board (PER Board), a seven-member board, appointed by the Governor. TRS is governed by the Teachers' Retirement System Board (TRS Board), a six-member board, appointed by the Governor. Teachers in school districts and some state institutions, excluding the faculty of the Montana University System (MUS), are covered by TRS, which is a DB plan. MUS faculty belong to the Montana University System Retirement Program (MUS-RP), a DC plan. The plan is governed by the Board of Regents (BOR).

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Investment Management

For the MPERA and TRS DB plans, assets are managed and invested by the Montana Board of Investments (BOI) as part of the state's unified investment program. For the PERS-DC plan, MPERA contracts with several retirement fund companies to provide a menu of investment options for plan members. For the MUS-RP, the Board of Regents contracts with the Teachers Insurance and Annuity Association (TIAA) for plan administration and investment options.

Constitutional Protections

Retirement fund assets, including contributions and investment earnings, are protected trust funds under the Montana Constitution.

Article VIII, Section 13

(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.

Article VIII, Section 15

(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.

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CHAPTER 4 – MONTANA LEGISLATIVE HISTORY RELATED TO PUBLIC RETIREMENT SYSTEMS

Recent Legislative History of Montana Public Retirement Systems

1997 is more or less considered the start of the modern pension era in Montana. In 1997, the financial markets were strong, and thus the pensions were more than fully funded, so the Legislature enacted a 1.5% Guaranteed Annual Benefit Adjustment (GABA) for the systems administered by MPERA. A 1.5% GABA for TRS was added during the 1999 session. In 2001, again in light of strong markets, the GABA was increased to 3.0% for both MPERA and TRS.

After the 2001 session, the financial markets took a sharp turn causing significant increases to the actuarial unfunded liabilities of the pension systems. By 2004, PERS did not amortize in any amount of time and TRS' amortization rate was over 70 years. The Legislature held a special session in December 2005 and approved a cash infusion of $25M to PERS and $100M to TRS.

In 2007, the Legislature decreased the GABA to 1.5% for new hires in the MPERA systems. They increased the employer contribution rate for TRS and added a $50M cash infusion (to TRS). In 2011, the Legislature reduced benefits and increased contribution rates for new hires in PERS and adjusted some benefit provisions in TRS.

In 2013, the Legislature passed what are considered the major pension reform bills of recent history*:

- HB 377 – Applies to TRS; creates two membership tiers; changes employee and employer contributions; reduces GABA for new, current, and retired members; establishes $25M supplemental funding; changes retirement and early retirement eligibility criteria; changes calculation for average final compensation; and changes eligibility for disability retirement; mandates yearly actuarial report to SAVA.
- HB 454 – Applies to PERS-DB; changes employee and employer contributions; appropriates unallocated portion of coal severance tax collections and revises the allocation of interest income from the coal tax permanent fund; and reduces GABA for new, current, and retired members.
- **The provisions of both bills changing benefits for existing members were challenged in court and subsequently struck down.*

In 2017, the Legislature passed HB 648, eliminating the coal tax appropriation to PERS and replacing it with a general fund statutory appropriation.

Treasure State Endowment Program

Mentioned above, HB 454 (2013) added an appropriation from the coal severance taxes and interest income from the coal permanent fund to PERS. To facilitate this, two Treasure State Endowment sub trusts – the Treasure State Endowment (TSE) Fund and the Treasure State Endowment (TSE) Regional Water System Fund – were sunsetted four fiscal years earlier than originally planned, ending in FY16

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rather than FY 20. As a result, the trust balances have not grown since FY 2016 and the interest income has remained relatively flat. In 2017, the Legislature passed HB 648 ending the appropriation from the coal severance taxes and interest income from the coal permanent fund and replacing it with a statutory appropriation directly from the general fund (no longer tied to coal revenues).

General Fund Contribution History

Statutory Appropriations from the General Fund to DB Pension Systems FY 2002 - FY 2022						
	TRS	PERS-DB	MPORS	FURS	HPORS	VFCA
2002			$ 6,529,108	$ 5,764,368		$ 1,133,741
2003			$ 6,798,457	$ 6,006,253		$ 1,310,088
2004			$ 7,208,135	$ 6,532,708		$ 1,434,068
2005			$ 7,704,884	$ 6,718,625		$ 1,527,264
2006			$ 8,181,861	$ 7,532,591	$ 813,429	$ 1,610,462
2007			$ 8,677,428	$ 7,957,373	$ 1,003,569	$ 1,660,695
2008	$ 13,492,375	$ 652,741	$ 9,451,808	$ 9,568,388	$ 1,106,188	$ 1,562,019
2009	$ 14,147,324	$ 685,704	$ 10,185,974	$ 9,831,417	$ 1,163,055	$ 1,579,887
2010	$ 17,241,610	$ 899,513	$ 10,931,612	$ 10,871,717	$ 1,327,062	$ 1,574,589
2011	$ 17,437,366	$ 920,805	$ 11,593,690	$ 11,365,441	$ 1,269,772	$ 1,596,436
2012	$ 16,843,766	$ 932,690	$ 12,273,769	$ 11,797,130	$ 1,469,539	$ 1,635,400
2013	$ 17,521,347	$ 940,919	$ 12,572,545	$ 12,357,856	$ 1,559,569	$ 1,711,321
2014	$ 42,855,576	$ 36,696,610	$ 13,048,938	$ 13,007,210	$ 1,618,559	$ 1,818,237
2015	$ 43,389,534	$ 32,458,886	$ 13,432,838	$ 13,572,990	$ 1,648,026	$ 1,913,482
2016	$ 43,902,606	$ 30,848,405	$ 13,751,561	$ 13,969,719	$ 1,715,507	$ 2,036,297
2017	$ 44,414,109	$ 28,807,314	$ 13,960,572	$ 14,438,412	$ 1,686,173	$ 2,064,561
2018	$ 45,005,672	$ 32,354,637	$ 15,857,660	$ 16,156,512	$ 1,709,764	$ 2,212,113
2019	$ 45,495,334	$ 33,073,273	$ 15,981,505	$ 16,605,850	$ 1,694,015	$ 2,370,449
2020	$ 45,948,388	$ 35,102,627	$ 16,636,173	$ 17,721,053	$ 1,709,685	$ 2,486,769
2021	$ 47,020,467	$ 35,494,697	$ 17,387,351	$ 18,437,718	$ 1,836,687	$ 2,591,791
2022	$ 47,999,500	$ 35,873,500	$ 18,122,207	$ 19,436,203	$ 1,864,976	$ 2,851,974

**NOTE: Some systems have multiple statutory appropriations; figures listed represent totals from all appropriations for each year. SRS, GWPORS, and JRS do not receive statutory appropriations.*

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CHAPTER 5 – DEFINED BENEFIT PLANS

How are Benefits Defined?

Defined Benefit (DB) plans provide a predictable formula-driven monthly benefit for the life of a member and sometimes for the life of a beneficiary. Benefits within a DB plan often also provide disability and death benefits. The traditional formula used to calculate the benefit amount paid in a DB plan is: Multiplier (%) x Years of Service x Final Average Salary.

Assets Invested in Pooled Trust Fund

To help pay for future benefits, current contributions are deposited into a pooled pension trust fund. The trust fund's assets are invested by the Montana Board of Investments (BOI). As the investments yield returns, the trust fund grows and must ultimately be sufficient to pay for benefits as members retire and the defined monthly benefits come due.

Determining Costs

The costs (i.e., how much employees and employers need to contribute to the plan to pay for future benefits) are estimated based on actuarial valuations. An actuarial valuation is a mathematical investigation by an actuary. These actuarial valuations assess the financial condition of the plan at a particular point in time. Montana law requires that actuarial valuations be conducted annually for each of Montana's DB plans. When estimating costs, actuaries evaluate whether current and expected contributions are sufficient to cover the estimated cost of benefits as they are expected to accrue and be paid in the future. The cost of benefits as they accrue is called the "normal cost." Other costs accrue when or if the experience of the plan is different from actuarial projections.

Actuarial Valuations & Experience Studies

Actuarial Assumptions

When making the projections that help determine the expected normal cost of benefits, an actuary applies various demographic and economic assumptions about future experience. Key demographic assumptions are made about the following:

- Individual salary increases
- Retirement rates
- Disablement rates
- Mortality rates
- Terminations of employment
- Probability of an employee retaining membership in system

Key economic assumptions are made about the following:

- General salary increases

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- Investment returns
- Price inflation
- Growth in membership
- Interest on member accounts
- Administrative expenses

Actuaries use economic and demographic assumptions when conducting actuarial valuations. These assumptions are developed based on a long-term analysis of actual experience based on standards adopted by the Actuarial Standards Board. The governing boards for the retirement systems set these assumptions based on the actuary's recommendations.

Current Economic Assumptions for Montana's Plans

ECONOMIC ASSUMPTIONS	MPERA SYSTEMS	TRS
Investment Rate of Return	7.30%	7.30%
Wage Growth	3.25%	3.50%
Inflation	2.75%	2.75%

Investment Rate of Return Assumption

Because retirement plans rely on investment returns for a significant portion of their funding, the most significant economic assumption actuaries make is what the rate of return will be on pension fund investments. An assumption that is too high will cause liabilities and funding needs to be understated, which means the plan's funding will likely be too low to keep the plan solvent. An assumption that is too low will cause liabilities and funding needs to be overstated, which places a burden on current employees and taxpayers to make higher contributions than necessary to keep the plan solvent. The investment rate of return assumption is the sum of two rates—an inflation rate and the real rate of return.

Actuaries for public employee retirement plans focus on a long-term investment horizon of at least 20 to 30 years, which is the typical length of an employee's working career and eligibility criteria for earning a full-service retirement benefit. Short-term volatility in the market does affect the funded ratio and amortization schedules for pension plan liabilities so a plan that is less than 100% funded will be more sensitive.

Experience Studies

Actuarial assumptions are tested and adjusted from time to time based on experience studies. An experience study examines the actual history and experience of the system and measures the assumptions against that actual history. Assumptions about mortality, disability, investment returns, and others, may then be adjusted accordingly. Montana law requires that regular experience studies be conducted for the statewide public employee retirement plans to compare actual experience with the actuarial assumptions. If plan experience shows that the actuarial assumptions need to be adjusted, an actuary will recommend that certain adjustments be made. The governing boards of the plans, who are the fiduciaries of the plan, set the assumptions after receiving recommendations from the actuary. Fiduciaries are legally and ethically accountable for their decisions.

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Amortization Period

A plan is considered actuarially sound if the unfunded liabilities are being paid for within a reasonable amount of time, or amortization period. In Montana, this is set at 30 years or less in 19-2-409, MCA.

Funded Ratio

Another key indicator of actuarial soundness is the extent to which current assets cover current liabilities. Current assets include the value of all of the trust fund's investments. Current liabilities include the value of all accrued benefit obligations. The ratio of assets to liabilities is called the funded ratio. If a DB plan has an unfunded actuarial liability, a DB plan's funded ratio will be less than 100%.

Annual Required Contribution (ARC)

Annual required contribution (ARC) refers to the total contribution needed (based on an actuarial valuation) to fund the normal cost of benefits as they accrue and to pay down the plan's unfunded liabilities in a reasonable amount of time.

Actuarial Gains and Losses

If actual experience is different from the assumed experience, the DB plan will have an actuarial gain or loss. For example, if investment returns are better than projected by the actuary, the actuarial valuation will show an actuarial gain equal to the amount that actual investment returns exceeded the actuarial assumed rate of return. If experience is worse than expected, then the retirement plan will have an actuarial loss. Each actuarial valuation includes a section about the plan's actuarial gains and losses.

Unfunded Liabilities

Actuarial losses or benefit increases applied to past service will result in an actuarial unfunded liability. Unfunded liabilities are typical in DB plans because projections cannot perfectly predict the future. Because these liabilities are typical, contributions to DB retirement plans should cover more than the normal cost of benefits. This allows the extra contributions to be made available to cover the ups and downs of the plan's experience. Thus, although these liabilities are called unfunded, if contributions are sufficient to pay more than just the normal cost of benefits, then the balance of the contributions after covering the normal cost fund the actuarial unfunded liabilities over time.

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CHAPTER 6 – DEFINED CONTRIBUTION AND HYBRID PLANS

Defined Contribution Plans

Defined contribution (DC) plans provide for a set contribution rate but do not promise a certain benefit at retirement. Plan members have individual accounts to which the contributions are made. The member then directs how those contributions are invested. Investment options available depend on what the plan sponsor provides. Each participant's account balance at retirement depends on total contributions plus investment earnings (or losses) to that point in time. When the participant retires, the balance of the account may be rolled over and reinvested or converted to a monthly annuity. Because contribution amounts are defined and costs are known, a DC plan has no unfunded liabilities and does not rely on actuarial projections about the future. In a DC plan, the employee is responsible for making investment choices and takes the risk of contributions plus investment earnings being insufficient to provide adequate income in retirement.

Hybrid Plans

Hybrid plans combine different elements of a DB plan and a DC plan. There are two broad categories of hybrid plans: cash balance plans and combination plans.

Cash Balance Plans

Under a cash balance plan, members have individual retirement accounts. Contributions, as in a DB plan, are set as a percentage of pay. Then, each account is credited with a certain amount of interest, as defined by the plan, depending on plan goals. The benefit ultimately paid, as in a DC plan, depends on the individual's account balance at retirement. However, as in a DB plan, the individual's account balance is a guaranteed amount based on the contributions and interest credited to the account, not on actual investment earnings. There are numerous variations of cash balance plans.

Combination DB/DC Plans

The most common hybrid plan is a combination DB/DC plan. Under this type of plan, part is a traditional DB plan, while the other part is a traditional DC plan. For example, the plan may provide that the employer contribution is deposited to a pooled DB plan trust fund, which guarantees a minimum benefit to the member. Meanwhile, the employee's contributions are deposited to the DC portion of the plan, which is an individual account invested by the employee in the investment options provided by the plan. At retirement, the member's benefit is the minimum DB benefit plus the member's DC account balance.

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Chapter 7 – Policy Principles, Policy Considerations, Risk Assessments, and the Role of the Legislature

Policy Principles

NASRA Recommended Retirement Principles

NASRA, the National Association of State Retirement Administrators, supports the following guiding principles to retirement security and public plan sustainability:

- Participation of all relevant stakeholders, including government employers, their plans, their employees, plan beneficiaries and retirees, and other taxpayers in discussions and processes about the design and financing arrangements of public retirement plans.
- Policy-driven decision-making that recognizes the retirement security and workforce management purposes of public employee retirement systems, and which is based on objective and pertinent information that fairly reflects the long-term time horizon and economic effects of public plan financing, benefit adequacy, and benefit distributions.
- Tailored solutions, achieved by affected stakeholders working through the state and local legislative and regulatory processes.
- Retention of core, indispensable elements of public plan design, namely, mandatory participation, shared financing, targeted income replacement, pooled investment and longevity risks, and lifetime benefit payouts.
- Removal of federal policy barriers to the preservation of these central retirement plan design features in the public sector and the adoption of federal policies that encourage their inclusion in the private sector.

Best Practices

The Government Finance Officers Association (GFOA) has published a summary of best practices on sustainable funding practices for DB plans, most of which are reflected in the funding policies adopted by the retirement boards administering Montana's plans. Board policies are posted on their respective websites. The GFOA best practices can be found here: https://www.gfoa.org/materials/responsible-management-and-design-practices-for-defined.

Policy Considerations

Past-Service Liability

Additional unfunded liabilities are created whenever a benefit enhancement is applied to past service. The liability occurs because the contribution rates for past service were set based on the projected costs of the previous benefits. A benefit enhancement increases the normal cost of the system going forward. But, if it also applied to service that was performed in the past, a past-service liability is created. One

way to avoid liability for past service is to make a benefit enhancement applicable only to new members.

Ratchet Effect

Just as a ratchet can be tightened but not loosened, legal protections related to contract rights often mean that once a retirement benefit is promised to members, it cannot be withdrawn from or reduced for those members. This is known as the "ratchet effect".

Leapfrog Effect

The "leapfrog effect" – granting benefit enhancements by allowing the retirement plans to play leapfrog with each other – can lead to inconsistent and inequitable retirement policy as well as additional costs and unfunded liabilities.

Funding Options

The following are funding mechanisms that can be considered when making changes to funding policy:

- Increase contributions to sufficiently fund the enhancement
- Extend the amortization schedule
- Apply the enhancement to new hires only

Fixing Funding Shortfalls

To address funding shortfalls, legislative options are limited to increasing contributions and reducing benefits. An employee's contributions may not be increased to an amount that is more than the normal cost of the employee's benefits, thus increasing the employer contributions or finding an additional source of funding are the primary options available. With respect to benefit reductions, courts have determined that because of contract rights, benefits cannot be reduced for current members, only for new hires. This means it will take about 10 to 20 years before the lower costs for reduced benefits will significantly help a plan's funding status.

Risk Assessments and Reporting Requirements

Adverse Experience

Due to significant market losses in 2001 and the financial crisis sometimes referred to as the 2008 Great Recession, public employee pension plans suffered serious investment losses. Negative market returns were dramatically lower than the actuarially assumed rate of return and unfunded liabilities increased significantly. To keep retirement plans solvent, many state legislatures, including the Montana Legislature, provided cash infusions, significantly increased contributions, and reduced benefits for future members. Thus, policymakers became aware of how sensitive public pension plans are to stress in the financial markets and to adverse plan experience compared to actuarial assumptions.

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Current Actuarial Reporting

Every annual actuarial valuation report includes a section detailing the plan's actuarial gains and losses in the last fiscal year. Every valuation also includes a section on the investment rate of return assumption and the plan's sensitivity to future experience if the investment return is above or below the assumed rate of return. Additionally, experience studies examine whether actuarial assumptions should be adjusted to better anticipate actual experience. Changes in assumptions, particularly in the investment rate of return assumption, will increase or decrease the actuarial liabilities of the plan and therefore change the contribution rate the actuary recommends.

Role of the Legislature

Fiscal Impact of Legislative Changes

In recent years, the Legislature has considered various pension reform bills seeking to redesign the DB plans to shift some or all of the risk and responsibility from the employer to the employee by creating hybrid plans or freezing the DB plans and moving employees to a DC plan. One of the key policy challenges legislators encounter when crafting reform bills is how to address the fiscal impact these reforms have on the long-term benefit obligations in the DB plans. Because DB plan funding relies on future contributions to meet funding obligations, if those contributions are diverted to the new plan or the horizon for realizing investment returns on those contributions is reduced, then the long-term experience of the plan will be fundamentally changed from the actuarial assumptions used when contribution amounts were set. Such changes will increase unfunded liabilities. Thus, any fundamental reform of the DB plans requires careful actuarial analysis and consideration of how to continue to pay for the DB plan's liabilities if employees (and the contributions for those employees) are moved out of the DB plan and into a DC or hybrid plan.

Fiscal Notes

The Governor's Office of Budget and Program Planning (OBPP), assisted by retirement system staff, prepares the fiscal notes for all retirement legislation with fiscal implications. Each fiscal note is required to show anticipated costs over the near term. However, the financial obligations incurred when retirement legislation is passed will be ongoing. In an effort to provide legislators and others with information necessary to make an informed assessment, the OBPP has developed a specialized format for fiscal notes prepared on retirement system-related legislation. Whenever retirement legislation with a fiscal impact is passed and the future of the affected retirement system is changed, an actuarial calculation is required in order to project the long-term costs.

Key funding information to look for in the fiscal note are:

- How will the normal cost of benefits be changed?
- Will new unfunded liabilities be created?
- How will the amortization period and funded ratio be affected?

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Legislative Options

What can legislators do with the information provided by risk assessments, stress tests, and sensitivity studies? The Legislature may enact legislation to revise the following aspects of a retirement plan and its funding going forward:

- contribution amounts;
- benefit amounts;
- plan design; and
- certain investment criteria.

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APPENDIX A – SAVA INTERIM COMMITTEE MEMBERS

Before the close of each legislative session, the House and Senate leadership appoint lawmakers to interim committees. The members of the SAVA Interim Committee, like most other interim committees, serve one 20-month term. Members who are reelected to the Legislature, subject to overall term limits and if appointed, may serve again on an interim committee. This information is included in order to comply with 2-15-155, MCA.

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APPENDIX B – PENSION ACRONYMS

- **457:** Deferred Compensation (457) Plan
- **AAL:** Actuarially Accrued Liability
- **ARC:** Annual Required Contribution
- **ASOP:** Actuarial Standards of Practice
- **COLA:** Cost of Living Adjustment
- **ERISA:** Employee Retirement Income Security Act of 1974
- **FAC:** Final Average Compensation
- **FURS:** Firefighters' Unified Retirement System
- **GABA:** Guaranteed Annual Benefit Adjustment
- **GASB:** Governmental Accounting Standards Board
- **GWPORS:** Game Wardens' and Peace Officers' Retirement System
- **HAC:** Highest Average Compensation
- **HPORS:** Highway Patrol Officers' Retirement System
- **IRA:** Individual Retirement Account
- **IRC:** Internal Revenue Code
- **JRS:** Judges' Retirement System
- **MBOI/BOI:** Montana Board of Investments or Board of Investments
- **MPERA:** Montana Public Employee Retirement Administration
- **MPORS:** Municipal Police Officers' Retirement System
- **MUS-RP:** Montana University System Retirement Program
- **PERS:** Public Employees' Retirement System
- **PERS-DB:** PERS Defined Benefit Retirement Plan
- **PERS-DC:** PERS Defined Contribution Retirement Plan
- **PER Board/PERB:** Public Employees' Retirement Board
- **SAVA:** State Administration and Veterans' Affairs Interim Committee
- **SRS:** Sheriffs' Retirement System
- **TRS:** Teachers' Retirement System
- **UAAL:** Unfunded Actuarially Accrued Liability
- **VFCA:** Volunteer Firefighters' Compensation Act

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APPENDIX C – PENSION GLOSSARY OF TERMS

- **401(k) Plan:** A defined contribution plan governed by section 401(k) of the Internal Revenue Code (IRC) that is offered to employees in the private sector. Employees voluntarily participate on an individual basis. A 401(k) allows an employee to set aside tax-deferred income for retirement purposes. In some 401(k) plans, the employer will match an employee's contributions dollar-for-dollar.

- **403(b) Plan:** A retirement plan governed by section 403(b) of the IRC that is similar but not identical to a 401(k) plan and is offered by nonprofit organizations, such as schools, universities, and some charitable organizations.

- **457 Plan:** A tax-exempt deferred compensation program governed by section 457 of the IRC that is made available to employees of state and federal governments and agencies. A 457 plan is similar to a 401(k) plan, except there are never employer matching contributions and the IRS does not consider it a qualified retirement plan.

- **Accrued Benefit:** A retirement, pension, or disability benefit that an employee has earned based on years of service. Accrued benefits are often calculated in relation to the employee's salary and years of service.

- **Accumulated Contributions:** The sum of all the regular and any additional contributions made by a member in a defined benefit plan, together with the regular interest on the contributions.

- **Active Member:** A member who is a paid employee making the required contributions and is properly reported for the most current reporting period.

- **Actuarial Accrued Liabilities (AAL):** The portion of liabilities that exceed of the present value of all benefits payable under a defined benefit retirement plan compared to the present value of future normal costs.

- **Actuarial Assumption:** An assumption applied by an actuary for the purposes of estimating benefit costs. Assumptions are demographic and economic and include variables such as life expectancy, return on investments, interest rates, and compensation.

- **Actuarial Cost:** The cost determined by an actuarial analysis to represent the present value of benefits.

- **Actuarial Valuation:** An analysis conducted by an actuary that helps estimate future costs or liabilities using economic and demographic assumptions. The assumptions are based on professional actuarial standards and involve a mix of statistical studies and experienced judgment.

- **Actuary:** An accredited professional with expertise in applying statistics, mathematics, and financial theory to quantify risk and uncertainty to determine liabilities and costs.

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- **Additional Contributions:** A member's payments to purchase various types of optional service credit.

- **Annual Required Contribution (ARC):** Annual Required Contribution rate necessary to amortize unfunded liabilities in a DB plan over the number of years set by the retirement board's amortization policy (e.g., 30 years) as determined by the system's actuary.

- **Annuity:** In the case of a defined benefit plan, equal and fixed payments for life that are the actuarial equivalent of a lump-sum payment under a retirement plan and as such are not benefits paid by a retirement plan and are not subject to periodic or one-time increases. In the case of the defined contribution plan, an annuity is a payment of a fixed sum of money at regular intervals, which may or may not be for life.

- **Amortization Period:** The amount of time required to pay off a retirement system's unfunded actuarial accrued liabilities, or UAAL, calculated by the retirement system's actuary based on projected contributions and investment earnings.

- **Benefit Recipient**: A retired member, a joint annuitant, or a beneficiary who is receiving a retirement allowance.

- **Closed Amortization:** Under this appraoch, the unfunded liability is amortized over a set number of years (ex: 30 years). Each year the unfunded liability is re-determined, reflecting any gains and losses that have occurred, and amortized in 1 fewer year (ex: 29 years, 28 years, etc.). Every year the amortization period gets shorter, until it reaches one year, at which point the unfunded liability has been paid off and the plan is fully funded.

- **Cost of Living Adjustment (COLA):** Increases in a retirement benefit amount, usually a percentage and based on national economic data, e.g., consumer price index.

- **Deferred Compensation:** An arrangement, subject to IRC conditions and requirements, in which a portion of an employee's income is paid out at a date after which that income is actually earned. The primary benefit of most deferred compensation is that any taxes due on the income are deferred until funds are withdrawn under the arrangement. A 457 plan is a deferred compensation plan.

- **Defined Benefit Plan (DB):** A pension plan in which a retired employee is entitled to receive upon retirement a regular, periodic, specific amount based on the retiree's salary history and years of service.

- **Defined Contribution Plan (DC):** A retirement plan in which the employee is required to or elects to contribute some amount of salary into an individual account over which the employee has some control for investing the assets and options when making withdrawals at retirement.

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- **Designated Beneficiary**: the person a member names to receive any survivorship benefits or lump-sum payments upon the member's death. Designated beneficiaries are either primary or contingent.

- **Direct Rollover:** A distribution from a qualified pension plan, 401(k) plan, 403(b) plan, and so forth, that is remitted directly to the trustee, custodian, or issuer of the receiving retirement plan or IRA and is reported to the IRS as a rollover.

- **Disability:** Total physical or mental incapacity of a member to do the essential functions of the member's job even with reasonable accommodations required by the ADA, for a permanent or extended and uncertain duration.

- **Early Retirement:** A retirement plan provision that allows an employee to retire before the normal retirement age or required years of service for a full retirement.

- **Employee:** A person employed in any capacity by a PERS employer who pays the person's salary.

- **Employee Retirement Income Security Act (ERISA):** The federal law enacted in 1974 that established legal guidelines for private pension plan administration and investment practices. Public retirement plans generally are not subject to ERISA.

- **Employer:** The state, its university system, or political subdivisions that contract with the Board to cover their employees under PERS.

- **Fiduciary:** A person or institution legally responsible for the management, investment and distribution of a fund. The trustees and administrators who are responsible for the oversight of employee benefit trust funds are considered fiduciaries. Fiduciaries are any person who (1) exercises any discretionary authority or control over the management of a plan or the management or disposition of its assets; (2) renders investment advice for a fee or other compensation with respect to the funds or property of a plan or has the authority to do so; or (3) has any discretionary authority or responsibility in the administration of a plan.

- **Funded Ratio:** The value of a pension plan's assets in proportion to the pension liability.

- **Government Accounting Standards Board (GASB):** An independent, private-sector organization based in Norwalk, Connecticut, that establishes accounting and financial reporting standards for U.S. state and local governments that follow generally accepted accounting principles.

- **Guaranteed Annual Benefit Adjustment (GABA):** An annual increase in the prior year's benefit amount, usually as a percentage of the benefit, similar to a cost-of-living adjustment.

- **Highest Average Compensation (HAC):** A member's highest average monthly compensation during a set period of consecutive months of membership service.

- **Inactive Member:** A member who terminates service and does not retire or take a refund of the

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member's accumulated contributions.

- **Individual Retirement Account (IRA):** A tax-deferred retirement account for an individual that permits the individual to set aside money each year, with earnings tax-deferred until withdrawals begin.

- **Internal Revenue Code (IRC):** Title 26 of the United States Code. It is also known as the federal tax code.

- **Layered Amortization:** This approach is considered a hybrid of open and closed amortization approaches. Similar to closed amortization, the initial unfunded liability is amortized over a set amount of time (ex: 30 years). Any gains or losses that arise in future years will be amortized over new amortization periods, which is similar to the open amortization approach. With each valuation, a new closed layer gets added to the amortization schedule. The amortization of the original unfunded liability and gains and losses from prior years remain unchanged, providing the expectation that the plan will become fully funded over the original amortization period if there are no significant gains or losses.

- **Member:** Any person with contributions and service on account with the PERS. Persons receiving retirement benefits based on previous service credit are also members.

- **Money Purchase Plan:** A type of defined contribution retirement plan in which the annual contribution amount is in proportion to the employee's wages and is mandatory every year.

- **Normal Cost:** An amount calculated under an actuarial cost method that is the estimated cost of the accruing benefits for members of a defined benefit retirement plan. It is determined for each valuation period. Normal cost does not include any portion of the supplemental costs of a retirement plan.

- **Normal Retirement Age:** The age at which a member is eligible to immediately receive a retirement benefit based on the member's age, length of service, or both, as specified under the member's retirement system, without disability and without an actuarial or similar reduction in the benefit.

- **Open Amortization:** Under this approach, the unfunded liability is amortized over a set amount of years (ex: 30 years). Each year the unfunded liability is re-calculated and amortized over a new set amount of years (ex: 30 years). This is the approach used in Montana with a 30-year amortization period.

- **Pension:** Steady income given to a person as the result of service (e.g., employee, military) that begins when a specific event (e.g., disability, retirement) occurs. Pensions are typically paid monthly and based on factors such as years of service and prior compensation. The payment may be made by a government, employer, pension fund, or life insurance company.

- **Portability:** The ability of an employee to retain benefits, such as in a pension plan or insurance coverage, when switching employers.

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- **Qualified Plan:** A plan that meets the applicable requirements of the Internal Revenue Code and, if applicable, the Employee Retirement Income Security Act. A qualified plan is eligible for favorable tax treatment.

- **Roth IRA:** A type of IRA established under the Taxpayer Relief Act of 1997 that allows taxpayers, subject to certain income limits, to save for retirement while allowing the savings to grow tax-free. Taxes are paid on contributions, but withdrawals, subject to certain rules, are not taxed.

- **Smoothing:** The process of amortizing investment gains and losses over a period of time to help reduce volatility in contribution rates.

- **Tax Deferred:** The payment of taxes in the future on income earned in the current period.

- **Termination or Termination of Service:** Means the member has left the employment relationship for at least 30 days, has no written or verbal agreement to return, and has been paid all compensation due, including but not limited to payment of accrued annual and sick leave. Upon termination, the member will cease to accrue benefits attributable to that employment.

- **Unfunded Actuarial Accrued Liabilities (UAAL):** The excess of a defined benefit retirement plan's actuarial liabilities at any given point in time over the value of its cash and investments on that same date.

- **Vested:** The status of a plan member who meets the minimum membership service requirement of the system or plan to which the member belongs and who is thus eligible to receive a benefit.

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APPENDIX D – HJ 8 STUDY RESOLUTION

A JOINT RESOLUTION OF THE SENATE AND THE HOUSE OF REPRESENTATIVES OF THE STATE OF MONTANA REQUESTING AN INTERIM STUDY OF MONTANA'S PUBLIC EMPLOYEE RETIREMENT SYSTEMS AND THE DEVELOPMENT OF RECOMMENDATIONS FOR A LONG-TERM STRATEGIC APPROACH TO FUNDING THE RETIREMENT SYSTEMS RECOGNIZING THE CONCERNS OF ALL STAKEHOLDERS, INCLUDING THE CITIZENS OF MONTANA.

WHEREAS, the Montana Legislature, by statute, determines the benefit structures and funding policies for nine statewide defined benefit retirement plans covering more than 52,000 active and 43,000 retired state, local government, and school district employees and involving more than $11.7 billion in assets and nearly $18 billion in liabilities; and

WHEREAS, of total annual contributions to Montana's eight cost-sharing defined benefit public employee retirement systems, more than $195 million is contributed by employees and nearly $240 million is contributed by employers; and

WHEREAS, nearly 60% of employer contributions to these retirement systems is paid by local governments and more than $180 million is paid from the state general fund through statutory appropriations and as supplemental contributions; and

WHEREAS, these contributions represent a significant investment for employees, local governments, school districts, and the state; and

WHEREAS, the state of Montana is fortunate to count among its many assets a committed and dedicated workforce and recognizes the value of retirement systems for compensating, recruiting, and retaining quality public employees who provide public safety, education, and other valued public services in our communities; and

WHEREAS, retirement benefits paid to Montana retirees have a significant economic benefit for local communities; and

WHEREAS, the state of Montana recognizes that governmental power is derived from the people and that the state has an absolute duty to protect the rights of its citizens and understands that all revenue used to pay for public services, including retirement system contributions, comes from and is derived from its citizens; and

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WHEREAS, it is in the best interest of our state and its future financial viability to ensure that recommendations related to its public employee retirement systems will not only support and promote necessary governmental services and the public employees who provide those services, but also recognize the financial burden placed on its citizens to support those services and employees.

NOW, THEREFORE, BE IT RESOLVED BY THE SENATE AND THE HOUSE OF REPRESENTATIVES OF THE STATE OF MONTANA:

That the Legislative Council be requested to assign the study pursuant to the ranking process described in section 5-5-217, MCA, to the State Administration and Veterans' Affairs Interim Committee and that the committee be requested to:

(1) study the financial stability of Montana's defined benefit public employee retirement systems;

(2) use the assistance of independent certified professional actuaries, if funding is made available by the Legislature for the actuarial services;

(3) investigate the actuarial impact on funded ratios and amortization schedules of alternative funding policies for determining required contributions and consider selected scenarios, recognizing the funding sources for and the relative health or weakness of these unique systems;

(4) review and study the governance structure of the public employee retirement systems;

(5) examine legislative education, oversight, and goals concerning the public employee retirement systems, including decision benchmarks or indicators for future action; and

(6) develop recommendations for a long-term strategic approach to setting contribution rates that will ensure the financial strength and resilience of the retirement systems while recognizing the responsibility placed on the taxpayers and citizens of this state.

BE IT FURTHER RESOLVED, that the State Administration and Veterans' Affairs Interim Committee invite two members of the Legislative Finance Committee, a Senate member and a House of Representatives member, one from the majority party and one from the minority party, to participate with, but not be voting members of, the State Administration and Veterans' Affairs Interim Committee on matters related to this study.

BE IT FURTHER RESOLVED, that the Legislative Services Division provide research, legal, and administrative staff support for the State Administration and Veterans' Affairs Interim Committee in accordance with section 5-11-112(1)(d)(i), MCA, and that the State Administration and Veterans' Affairs

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Interim Committee presiding officer may request that the Legislative Fiscal Division provide fiscal analysis as needed in accordance with section 5-12-302(5), MCA.

BE IT FURTHER RESOLVED, that the study be conducted and the recommendations be developed in consultation with all interested stakeholders, including but not limited to representatives of:

(a) the state's taxpayers;

(b) active and retired members of the retirement systems;

(c) employers, including local governments, school districts, and state agencies;

(d) key agencies, including the Governor's office, the retirement boards, and the Board of Investments; and

(e) other interested parties as considered appropriate.

BE IT FURTHER RESOLVED, that all aspects of the study, including presentation and review requirements, be concluded prior to September 15, 2022.

BE IT FURTHER RESOLVED, that the final results of the study, including any findings, conclusions, comments, or recommendations, be reported to the 68th Legislature.

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APPENDIX E – HJ 8 STUDY MATERIALS

The following materials were prepared for the SAVA committee during the course of the HJ 8 study:

- FY22 Green Sheets: https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/FY22-Green-Sheets-NEW.pdf
- May 2022 Pension Funding History and Spreadsheet of Statutory Appropriations: https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/Tab8-Pension-Funding-History.pdf
    - Individual System General Fund Contributions: https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/Individual-Pension-Systems-Funding-History.pdf
- March 2022 Staff Briefing Paper – Pension Plan Design: https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/Tab7-Staff-Briefing-Paper-Pension-Plan-Design.pdf
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- December 2021 Staff Briefing Paper: Game Wardens' and Peace Officers' Retirement System (GWPORS) Overview: https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/Staff-Briefing-Paper-GWPORS.pdf
- FY21 Green Sheets: https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/Tab7-FY21-FINAL-Green-Sheets.pdf
- November 2021 10-State Comparison Spreadsheet: https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/10-State-Comparison-Chart.pdf
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