

State Pension Practices and Considerations for Montana

Montana SAVVA
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Pew

Overview

- Information on Pew retirement security metrics
- Examples of state pension practices
- Defining the problem for Montana policymakers
- Potential approaches

Information on Pew Retirement Security Metrics

Replacement Income Comparison

Defined benefit plans paired with Social Security have the highest level of replacement of take-home pay.

Type of Plan	In Social Security	Number of Plans Covered	Plans with more than 100% replacement	Plans between 100% and 90% replacement	Plans between 90% and 80% replacement	Plans below 80% replacement
Defined Benefit	Yes	43	21	17	4	1
	No	15	0	2	3	10
Hybrid	Yes	12	5	2	3	2
	No					
Cash balance	Yes	4	2	0	0	2
	No					
Defined contribution	Yes	4	0	0	0	4
	No	2	0	0	1	1

Name	In Social Security	Replacement Rate	Adjusted For Inflation	With Social Security	Adj for Take Home Pay	Rank among DB w/ Social Security
Montana PERS	Yes	66%	61%	94%	112%	12
Montana TRS	Yes	55%	51%	84%	100%	22

Source: State annual financial reports, pension plan financial reports, and plan actuarial valuations

Saving Rate Comparison

MT PERS was one of just seven state plans providing at least 12% savings for mid-career workers

- State workers in Montana get a benefit that is the higher of the final average salary formula or their accumulated employee contributions matched by equivalent employer contributions plus interest converted to an annuity.
- Similar provisions support workers in CO, SD, and WI.
- This type of benefit helps maintain non-career workers in final average salary defined benefit plans on a path to retirement security.

Members hired **on or after** July 1, 2011:

- Less than 10 years of membership service:
1.5% of HAC x years of service credit
- Between 10 and 30 years of membership service:
1.785% of HAC x years of service credit
- 30 years or more of membership service:
2% of HAC x years of service credit
- **OR**, if greater than any of the above:
the actuarial equivalent of 2 times the member's regular contributions and interest plus the actuarial equivalent of any additional contributions and interest.

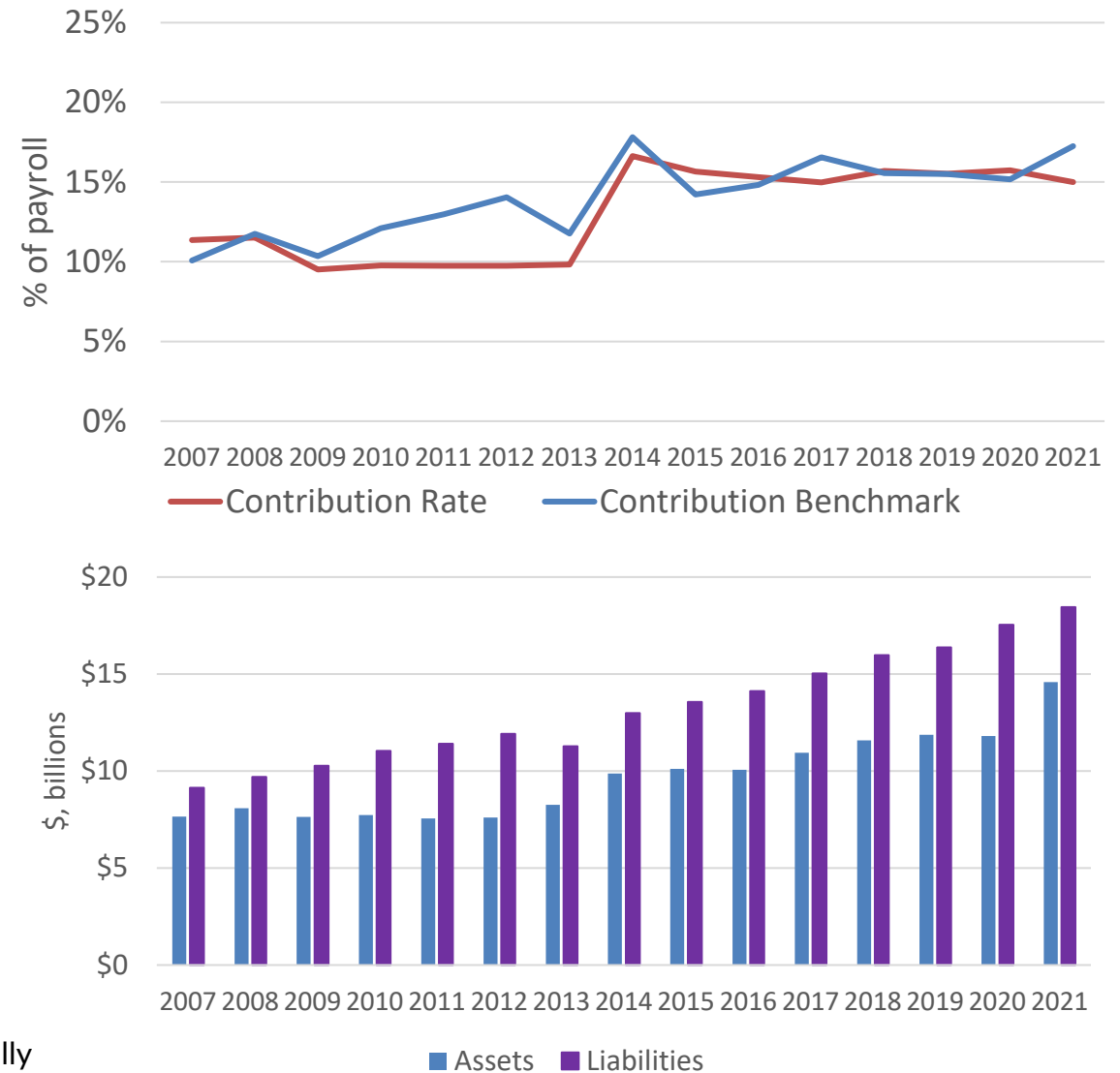
Source: MT PERS 2023 Actuarial Valuation

Note: Pew's savings rate analysis examines retirement security outcomes for plans in which members participate in Social Security.

Examples of State Pension Practices

Montana

- Montana’s fixed contribution policy has lagged contribution benchmarks in **9 of the last 15 years**.
- The 2014 increase in contributions and other changes helped address this—contributions matched benchmarks in 5 of the last 8 years.
- **Montana doesn’t have policies that would effectively respond to a future downturn.**
- The following state examples show the range of approaches that states have used to try to manage investment volatility and other challenges to sustainability.

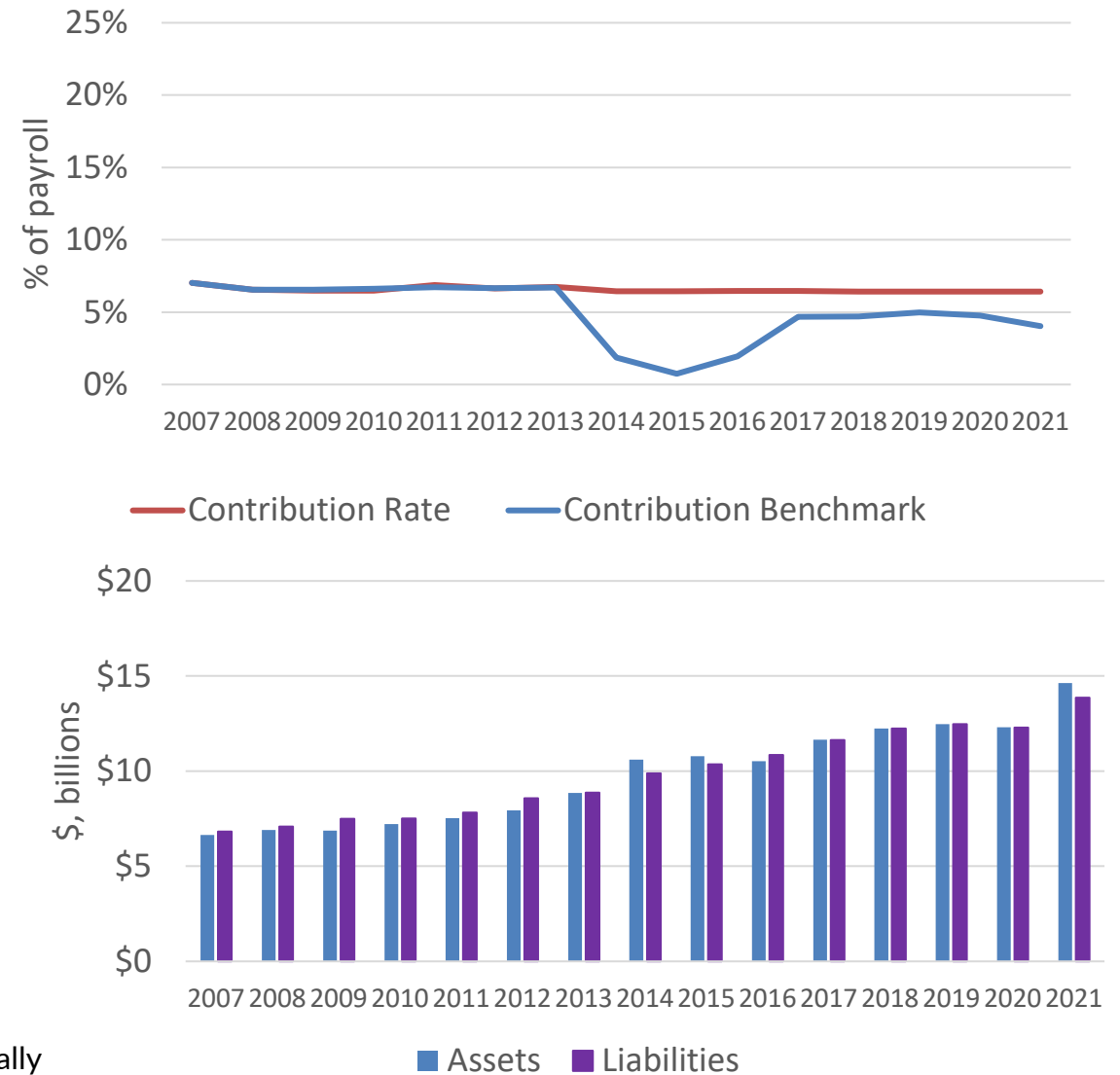


Note: In the contribution chart, the contribution benchmark pre-2014 is the actuarially determined employer contribution and for 2014 onwards is the Net Amortization Benchmark.

South Dakota

- Final average salary defined benefit with 1.8% multiplier.
- Fixed contribution policy with adjustable benefits.
- The maximum allowable COLA is adjusted annually to ensure the statutory contribution rate is actuarially sufficient.
 - Maximum COLA can be no higher than 3.5% and no lower than 0%.
 - As of 2023 valuation, maximum allowable COLA is 1.9%.
 - COLAs accrue at separation, not at retirement, helping protect non-career workers from inflation.

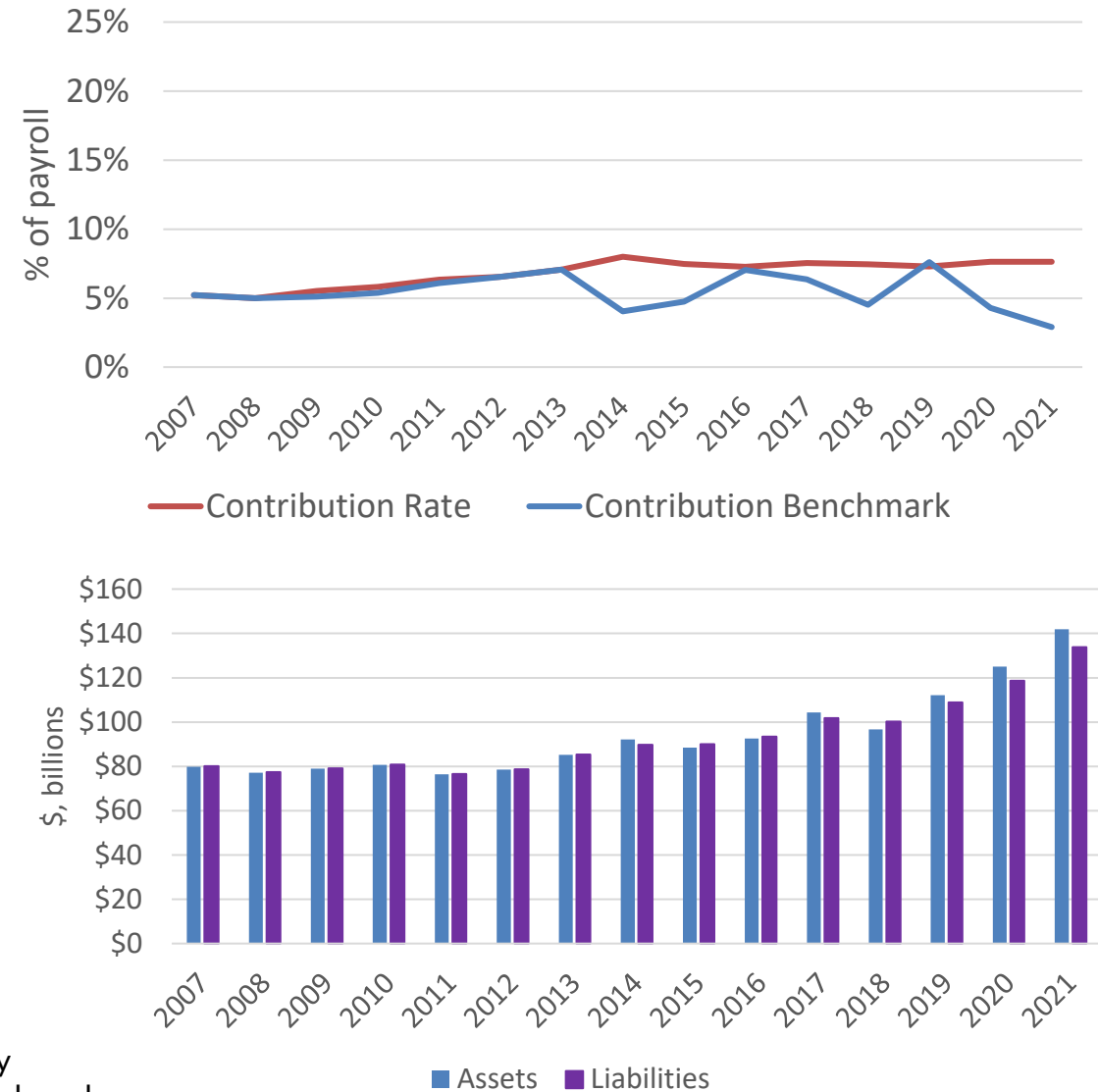
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Wisconsin

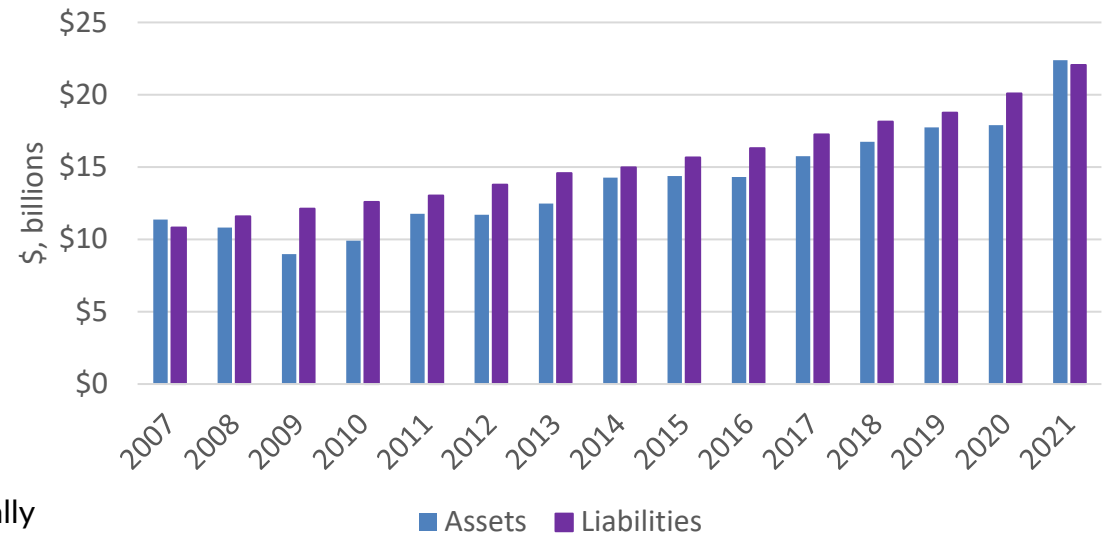
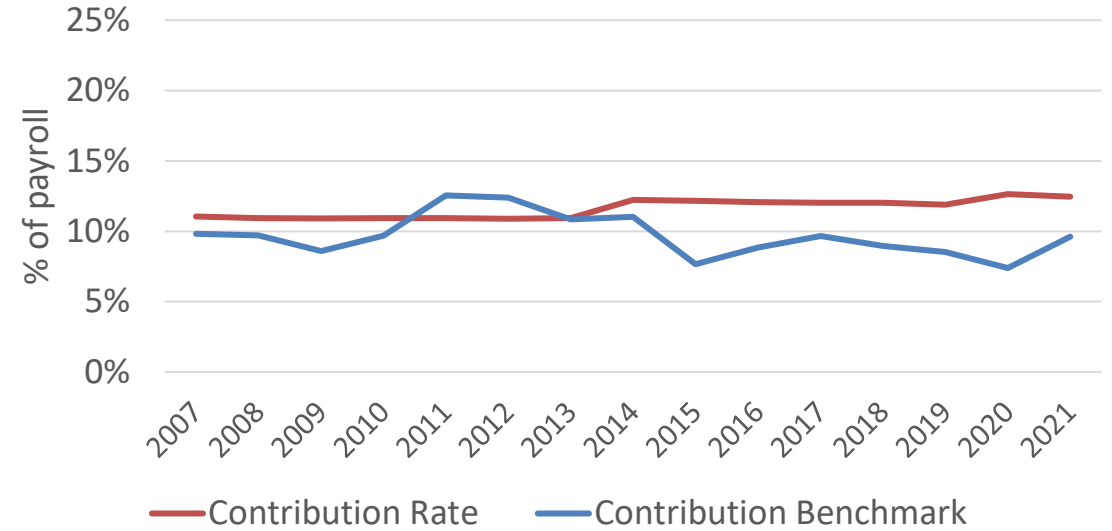
- Wisconsin follows a shared-risk defined benefit funding model.
- Liabilities are actuarially funded, with contributions split between employer and employee.
- Retiree COLAs are adjusted to ensure that the assets set aside to pay for retiree benefits will match the cost of those liabilities.
- COLAs can be suspended or reduced per that risk-sharing policy, but Wisconsin retirees also received benefit adjustments of 5.1% and 7.4% in 2020 and 2021.

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Idaho

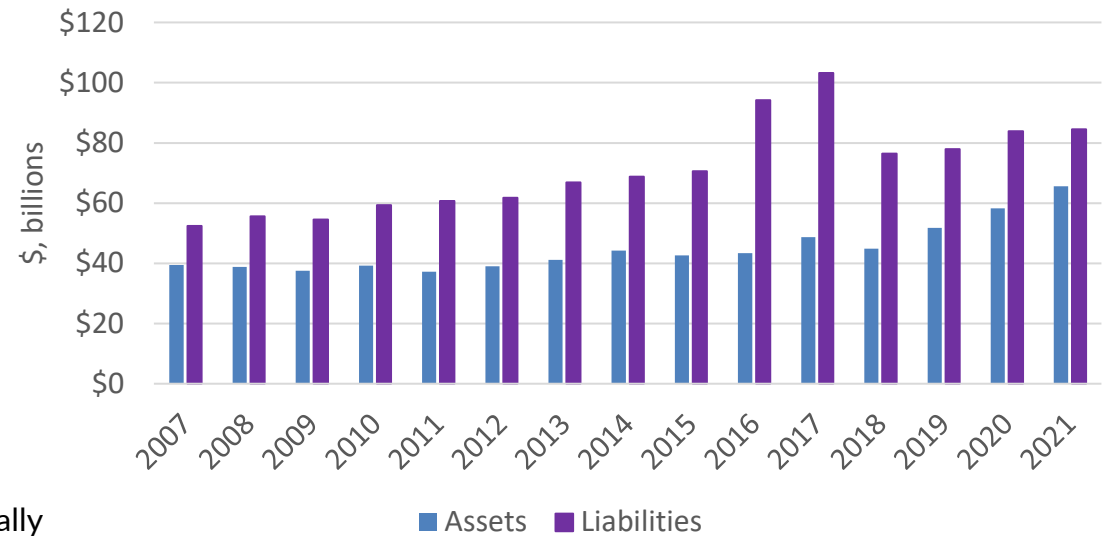
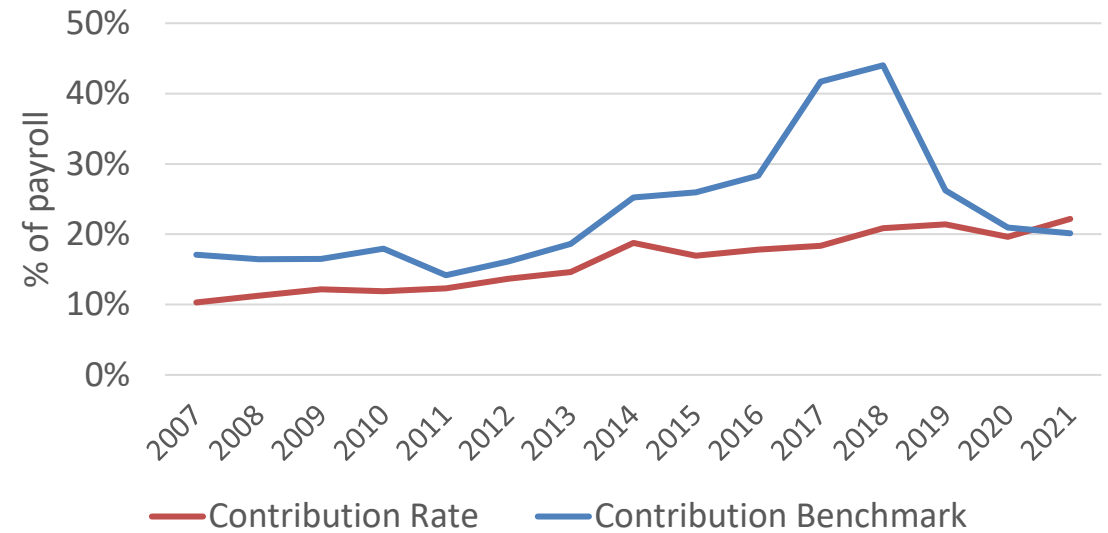
- Idaho’s contributions have, on average, exceeded minimum benchmarks, allowing funding to recover from the Great Recession.
- The board sets funding policy based on statutory goals for amortization. Contribution rates are typically set above those minimum thresholds to build a buffer.
- Employee contribution rates are set at a fixed share of the employer rate, ensuring that losses are shared as well as gains.



Note: In the contribution chart, the contribution benchmark pre-2014 is the actuarially determined employer contribution and for 2014 onwards is the Net Amortization Benchmark.

Colorado

- In 2016, a Colorado pension stress test showed a 1 in 4 chance of insolvency due to an insufficient fixed contribution policy.
- Lead to changes with shared sacrifice through higher employer and employee contributions and a lower COLA.
- If those changes prove insufficient, the policy will automatically adjust through additional increases in contribution rates and a further COLA reduction.
- The state mandated regular stress testing due to its value as an early warning signal.

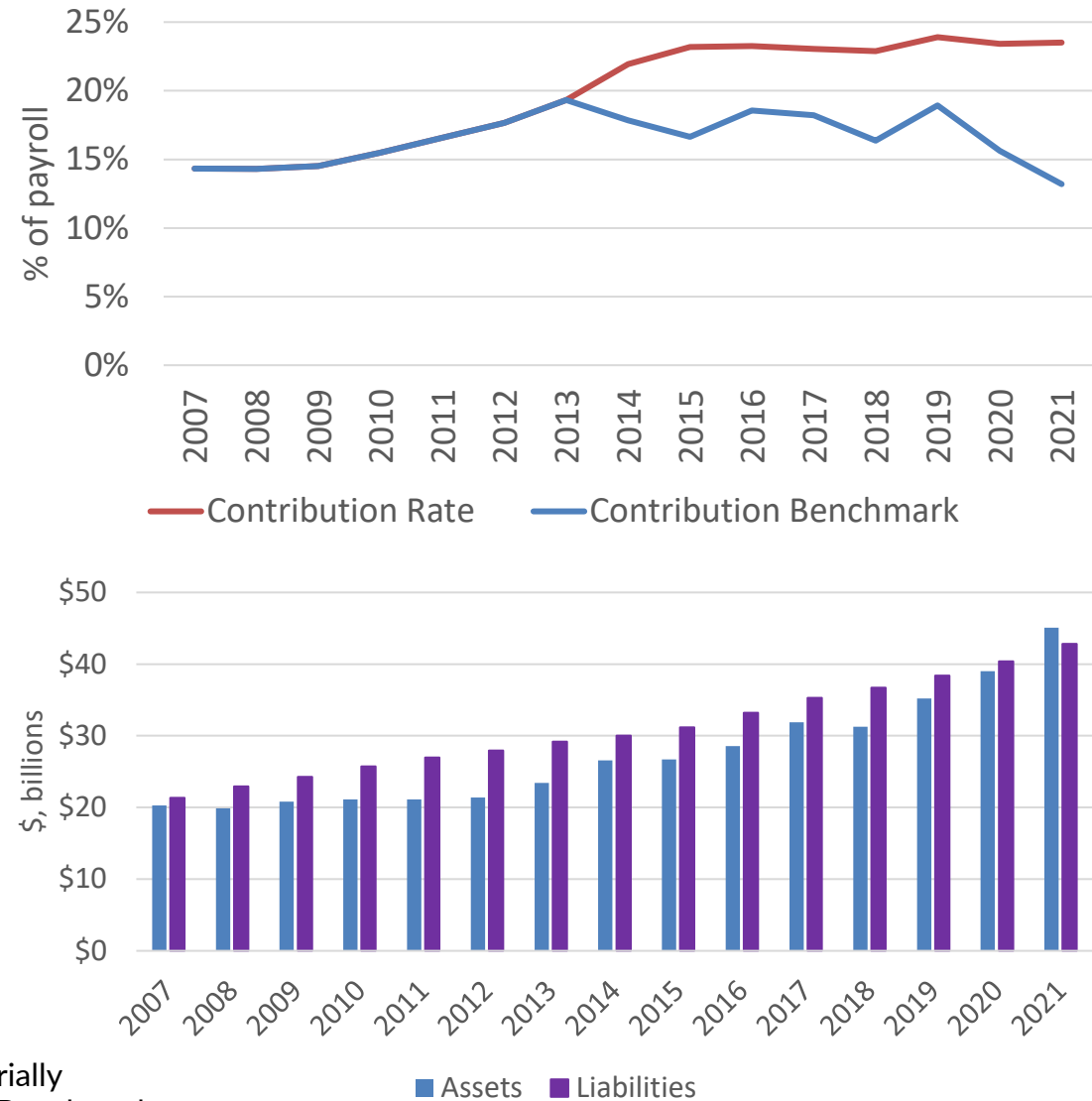


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Utah

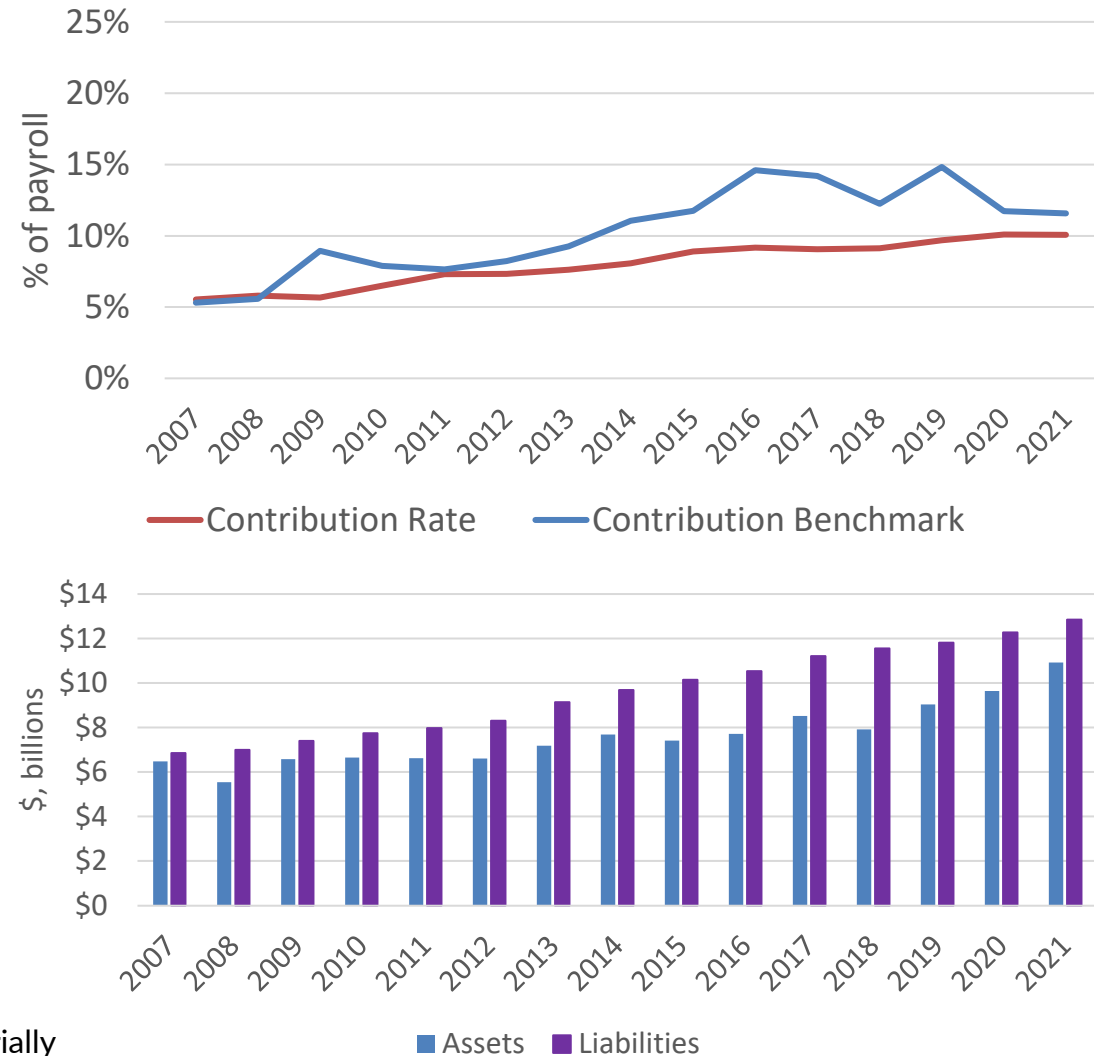
- Utah faced a drop in funded ratio and increase in the employer contribution rate following the Great Recession.
- Actuarial funding allowed the funding situation to recover but policymakers wanted to reduce future risk.
- The new plan design is a hybrid with a 1.5% multiplier and a fixed employer cost of 10% of payroll.
 - If actuarial costs for the DB portion of the hybrid exceed 10%, employee contributions will make up the difference.
- Utah’s funding policy will maintain a buffer when times are good.

Note: In the contribution chart, the contribution benchmark pre-2014 is the actuarially determined employer contribution and for 2014 onwards is the Net Amortization Benchmark.



Wyoming

- Wyoming has seen actual contributions consistently fall short of the contribution benchmark since the Great Recession.
- This has been paired with a growing gap between assets and liabilities—even after strong 2021 returns, the state’s pension liabilities were just 85% funded.
- Starting in 2026, Wyoming will commit to following an actuarial contribution policy.

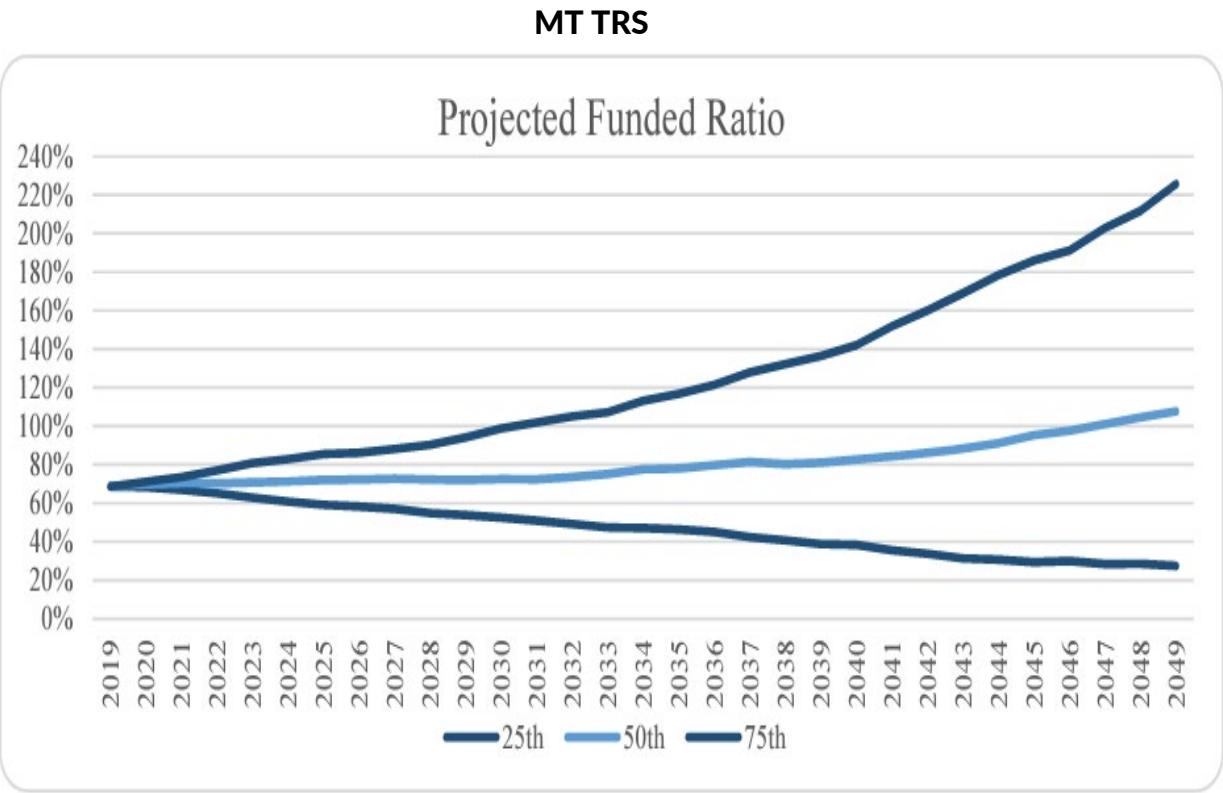
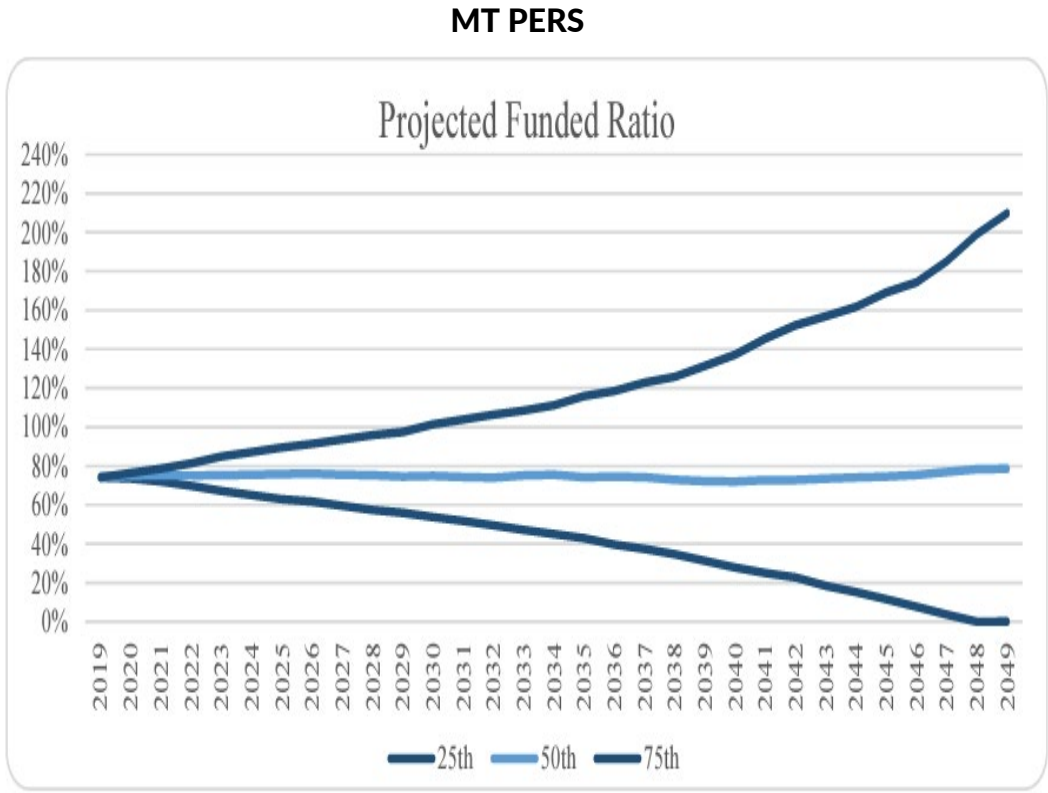


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Defining the Problem for Montana

Montana's Policies Don't Adjust for Risk

Current policy leads to risk of significant underfunding and insolvency



Note: Based on 2020 Cavanaugh MacDonald Risk Analysis Reports for MT PERS and MT TRS.

What Does Montana Need for Pension Sustainability?

- Assuming investment returns go as expected, Montana's current policies are sufficient to pay down the unfunded liability for PERS by 2051 and for TRS by 2046.
- As the results of the most recent stress tests show, PERS had a 1 in 4 chance of insolvency by 2049 while TRS would have significant drops in the funded ratio in that scenario.
- States use a range of tools to manage investment volatility and other risks including actuarial contribution policies that adjust to pension funding needs and adjusting COLAs and other benefit provisions based on investment performance.
- Montana has a number of examples to draw from in considering how to address this challenge.

Actuarial Funding and Budget Risk

- If Montana sets an actuarial funding policy that will automatically adjust to funding needs, how can policymakers insulate against the risk of budget crowd-out?
- States have options in setting an actuarial contribution policy designed for stability and predictability and can add risk management policies to further reduce volatility.
- Contribution policies can build buffers against volatility to keep costs stable.
 - CT—extra payments when times are good; UT—limit annual reduction in contribution rates; TN—reserve fund
- Alternative plan designs and risk-sharing policies can help ensure predictable contribution rates.
- Statutory funding policies can work if automatic adjustments make sure contributions meet funding needs.
 - SD—COLAs adjust to match contributions to actuarial rate; CO—automatic adjustment to employer and employee contributions and COLAs

Options for Consideration

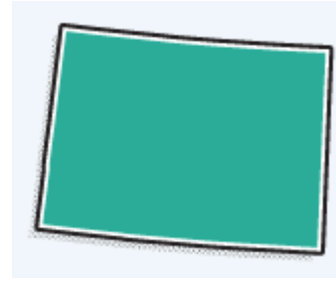
- **Shared-risk Defined Benefit** (Example state: Wisconsin)
- **Automatic Adjustment** (Example states: Colorado, South Dakota)
- **Risk-managed Hybrid** (Example states: Tennessee, Utah)

Shared-risk Defined Benefit



- Actuarial funding policy to ensure long-term sustainability.
 - Layered amortization to ensure unfunded liabilities are paid off while minimizing contribution volatility.
- Contribution rates shared between employer and employee.
 - As funding levels improve, employee contributions are lowered.
- COLAs depend on investment performance rather than the funding of legacy liabilities.
- Extend the employer contribution matching benefit to TRS members.

Automatic Adjustment



- Set statutory contributions at a sufficient level to be adequate to fund benefits with some cushion for lower-than-expected returns.
- Identify a threshold at which changes should be made—either based on amortization period or by comparing contribution rate to ADEC.
- Set automatic changes to employer contributions, employee contributions, and COLAs to ensure fiscal sustainability if threshold is met.
- Conduct regular stress testing to determine whether baseline policies and automatic adjustments are sufficient to manage a range of scenarios.

Risk-managed Hybrid



- Reduce multiplier for new hires to 1% or 1.5%—commit to actuarially funding that benefit.
- Add a defined contribution or cash balance benefit to supplement the defined benefit.
- Set employer contributions to DB plan above expected actuarial cost to create a buffer against volatility. Set employee contributions to vary based on investment returns.

Conclusion

- Montana's benefits for career workers are within the range we see for DB plans where members participate in Social Security. The MT PERS benefits include an employee contribution matching provision that sets a savings floor.
- States follow a range of approaches to ensure pension policies are sustainable in the face of investment, demographic, and other uncertainty.
 - Included in those practices are tools to manage risk and ensure predictable costs.
- **Montana's central pension policy challenge is to ensure there is an answer for what happens if investments fall short of expectations.**
- We presented three options for consideration about how to apply some of the lessons from the state examples to Montana.
- **There is no one-size-fits-all solution and instead multiple proven approaches that allowed states like SD, TN, and WI to ensure well-funded benefits with stable costs.**

For more information:

<https://www.pewtrusts.org/en/projects/public-sector-retirement-systems>

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