



State Administration and Veterans' Affairs Interim Committee

59th Montana Legislature

SENATE MEMBERS

JOSEPH TROPILA--Vice Chair
BILL TASH--Chair
KEITH BALES
CAROLYN SQUIRES

HOUSE MEMBERS

RALPH HEINERT
VERDELL JACKSON
RALPH LENHART
VERONICA SMALL-EASTMAN

COMMITTEE STAFF

DAVE BOHYER, Lead Staff
JOHN MACMASTER, Staff Attorney
FONG HOM, Secretary

MINUTES

Please note: These are summary minutes. Testimony and discussion are paraphrased and condensed. Committee tapes are on file in the offices of the Legislative Services Division. **Exhibits for this meeting are available upon request. Legislative Council policy requires a charge of 15 cents a page for copies of the document.**

Please note: These minutes provide abbreviated information about committee discussion, public testimony, action taken, and other activities. The minutes are accompanied by an audio recording. For each action listed, the minutes indicate the approximate amount of time in hours, minutes, and seconds that has elapsed since the start of the meeting. This time may be used to locate the activity on the audio recording.

An electronic copy of these minutes and the audio recording may be accessed from the Legislative Branch home page at <http://leg.mt.gov>. On the left-side column of the home page, select *Committees*, then *Interim*, and then the appropriate committee.

To view the minutes, locate the meeting date and click on minutes. To hear the audio recording, click on the Real Player icon. Note: You must have Real Player to listen to the audio recording.

April 21, 2006

Capitol Building, Room 102
Helena, Montana 59601

COMMITTEE MEMBERS PRESENT

SEN. JOSEPH TROPILA, Acting Chair

SEN. KEITH BALES

REP. RALPH HEINERT
REP. RALPH LENHART
REP. VERONICA SMALL-EASTMAN

COMMITTEE MEMBERS EXCUSED

REP. VERDELL JACKSON

COMMITTEE MEMBERS ABSENT

SEN. CAROLYN SQUIRES

STAFF PRESENT

DAVE BOHYER, Lead Staff
JOHN MACMASTER, Staff Attorney
FONG HOM, Secretary

Visitors

Visitors' list, [Attachment #1](#).

COMMITTEE ACTION

- Guidelines 1 through 26 with the exception of Guideline 20 was adopted.
- Dave Bohyer will draft a letter to PERB, with a copy to TRB, requesting numbers and what would happen to employers and the contribution to keep the current system actuarially sound if new hires were put into the Defined Contribution Plan and not into the Defined Benefit Plan.

PART 1 TAPE 1A

00:00:02 CALL TO ORDER AND ROLL CALL

SEN. TROPILA called the meeting to order at 8:30 a.m. Secretary took roll. Sen. Tropila told the Committee that Sen. Tash has resigned from the SAVA Committee due to health reasons. Rep. Jackson was excused; Sen. Squires was absent.

00:01:10 The March 6, 2006 minutes were approved and accepted unanimously.

00:01:31 OVERVIEW OF PRINCIPLES, POLICY GUIDELINES - Dave Bohyer, Lead Staff, LSD

Mr. Bohyer presented the Principles and Guidelines for Montana's Public Employee Retirement Systems (**EXHIBIT 1**). He said that this Committee is charged with establishing the policy and guidelines in Montana under Section 5-5-228, MCA, as revised in the December 2005 Special Session.

TAPE 1B

00:45:45 REP. LENHART asked for clarification of the phrase "*in retirement* means at the completion of a working career, not at the end of employment", found in Parsing Principle 1. MR. BOHYER said that when some state employees eventually retire from state government, they probably will still go on and work somewhere else. What is suggested is that the retirement benefit should kick in when a person actually stops working, not just from working at his or her employment with the public entity that is the sponsor of the plan.

00:48:04 REP. HEINERT asked if the contribution rates can be changed upward for current and future employees as well as the employers, or is it just for future employees. MR. BOHYER said that the answer is yes, but there is a qualifier. You can change the employees' contribution for current employees if you add additional benefits. You can change the employees' contribution for future employees regardless of what you do with the benefit.

REP. HEINERT asked if the cost of living increases can be reduced for current employees. MR. BOHYER said that, no, there are constitutional impairment of

contract issues that come up with that, and those impairment of contract issues arise under both the federal constitution and the state constitution.

00:50:24 SEN. BALES asked in regard to the suggestion that the legislature have its own actuary if the PERS does an actuarial valuation biennially and TRS does it annually. MR. BOHYER said yes, and that the frequency of the actuarial valuations is something that the Committee discussed at prior meetings and stated in reports that he had sent out.

00:53:49 MR. MACMASTER asked if the one-time, *ad hoc* benefit increases should not be enacted, and does that mean it shouldn't be enacted without adequately funding them at the time of enactment. MR. BOHYER said that it means that if you do the benefit increase, you have violated the principle that says your funding should be contemporary because the funding that would have been able to pay for that over time was not paid for by those employees, employers, or taxpayers for the employees who would get the adjustment.

00:55:34 **MS. ROXANNE MINNEHAN, Executive Director, Montana Public Employees Retirement Association**

MS. MINNEHAN discussed some of the guidelines and principles that the Montana Public Employees Retirement Board uses in reviewing legislation. She submitted written testimony that included comments regarding Mr. Bohyer's presentation; their Principles and Guidelines; PERB Funding and Benefit Policy; Retirement Legislation Decision Points; Gabriel, Roeder, Smith & Company/National Association of State Retirement Administrators joint letter to Michael H. Moskow (**EXHIBIT 2**).

01:06:12 SEN. BALES asked when the Retirement Legislation Decision Points came about. MS. MINNEHAN said that she is not sure when that was devised, that it was given to her by Kelly Jenkins, their attorney.

SEN. BALES asked regarding the statement "that by requiring all new hires to go to a Defined Contribution Plan, you were then jeopardizing the retirement funds for existing employees": how will switching all new hires to a Defined Contribution Plan hurt the current employees? MS. MINNEHAN said that the reason for that is because the DB Plan pools the employer contributions into the system that fund the system; the actuary is looking at the entire pool of contributions coming in for future retirees.

SEN. BALES asked that if the employer continues to pay and the employee continues to pay into the fund and there were no new hires, and you were current

on your funding, would we have to raise the employer's contribution in order to make that work. MS.MINNEHAN said yes, and because you have those current members, that liability is still there.

01:11:58 REP. HEINERT asked, if you infuse funds enough to make the current system actuarially sound, would you have to increase the employer contribution if you were going to change future employees to a Defined Contribution Plan. MS. MINNEHAN said that it depends by what your definition of actuarially sound is because you can amortize those unfunded liabilities over 30 years and still be actuarially sound, so you still have those unfunded liabilities out there.

01:13:42 SEN. BALES said that he is sitting here thinking where we are saying that we are actuarially sound at 30 years, in essence, that is saying that we are not doing a pay as you go, because most careers are probably not 30 years. How many years, instead of 30, would we need to take it down to, to be on a pay as you go for a Defined Benefit Plan. Do you have that figure, or do you have any idea what that would be. MS. MINNEHAN said that she doesn't have any figures, but she said that you would at least have to take it to where there is no unfunded liability.

SEN. BALES said that his question is, if you are amortizing it or figuring it over a 30-year period, by having a 30-year period on that, are we in essence deferring some of that liability to future workers, and if we are, do we need to bring that 30-year back to 25 or 20, and stop deferring it on the future employees or into the future. MS. MINNEHAN said that she would have to confer with their actuary on that.

01:16:14 **DAVID SENN, Executive Director, Montana Teachers' Retirement System**
Mr. Senn distributed to the committee his comments regarding Mr. Bohyer's presentation on Principles, Policy Guidelines, and Policy Statements for Public Retirement Systems (**EXHIBIT 3**).

TAPE 2A

01:36:21 SEN. BALES asked, if you were going to do an increase in the GABA, what is the number of years, a pay as you go, that would satisfy that the pension funds were being paid for instead of putting it on the future hires. MR. SENN said that first of all, the system will never be pay as you go. Sixty-two percent of teachers retirement benefits are paid by investment earnings. We need a large pool of assets, pre-funding benefits, if interest earnings are going to pay for those benefits. It is always going to be a pre-funding retirement benefit.

01:42:35 REP. HEINERT asked if the amount of the underfunded Teacher Retirement System of \$900+M was infused, does that mean that it would be actuarially sound at zero, and it wouldn't be 30 years. MR. SENN said that was correct.

01:43:43 **CARROLL SOUTH, Executive Director, Montana Board of Investments**
MR. SOUTH discussed the review of the 1995 report, written at the time the stock market was taking off, and the 2000 report, written when the market had already started to tank and 6 of the 9 pension funds had an actuarial surplus. Mr. South said that he only has two principles for the Legislature: **PRINCIPLE 1.** The Legislature should always increase benefits commensurate with increasing the contributions. **PRINCIPLE 2.** Don't encourage early retirement under the guise of saving general fund money.

01:55:38 SEN. TROPILA asked if Mr. South is espousing a rainy day fund that should be earmarked if in the future there is a surplus. MR. SOUTH said that his recommendation is, don't start increasing benefits using the unfunded liability when you get the amortization down to 15 years, because by doing so, you have reduced your margin of error.

01:57:25 SEN. BALES asked Mr. South where your fund was at, your investments were at before the crash that we had in 2001, 2002. He asked what are the numbers now as compared to then. MR. SOUTH said that in 2003, the return was almost 8%; in 2004, it was 13%; in 2005, it was 8%. He said that he anticipates over a long period of time that we can still earn 8% return and the 7.75% for teachers.

01:59:03 DAVE BOHYER asked Mr. South to comment on the asset/liability modeling of the TRS and PERS. MR. SOUTH said that one of the things that has never occurred with the state's pension plans is an asset/liability study where you look at both components at the same time. Mr. South talked about having a document telling us how we should properly allocate assets to meet the liabilities. This will be presented at the Board of Investments' meeting on May 18.

BREAK

02:21:34 **RANDY MORRIS, Administrator, Personnel Division, Department of Administration**
MR. MORRIS commented on the impact on the work force that results from what the Committee does. Mr. Morris also distributed copies of the Employee Profile from the Department of Administration, State Personnel Division (**EXHIBIT 4**) to the committee members.

TAPE 2B

- 02:34:22 SEN. TROPILA asked if the report included the retirees from city/county employees. MR. MORRIS said that it did not.
- 02:34:36 **TOM SCHNEIDER, Montana Public Employees Association**
MR. SCHNEIDER said that the Guidelines are good but he would add to that, for this time in history, and there should be one additional guideline that says, these guidelines will be reviewed and updated, and time changes everything. He said that if you look at the survey handed out, 34% of the employees are making a retirement decision based on whether the Legislature is going to grant an early retirement.
- 02:37:17 REP. HEINERT asked Mr. Schneider what the impact would be on the DB Plan if those contributions all went back into the DC plan where they should be going now. MR. SCHNEIDER said that the purpose of the plan choice rate was to fill the void created by DB plan members switching to the DC plan. Today in PERS, the normal cost is 12.12%. The contributions being paid are 13.8%. That leaves 1.64%, the difference between normal costs and the contribution rate that was to pay off the unfunded liability. That unfunded liability was there when the Defined Contribution rate was put in place and when the defined contribution went into effect, the employees who switched to the DC plan and those who would initially choose the DC plan would no longer be paying the additional amount for the unfunded liabilities. If you stop the Defined Benefit Plan and put everyone into the Defined Contribution Plan, and you didn't have a 100% funded system, which we don't have, then you would create a huge hole and that unfunded liability would escalate because we are not getting that money that is paying off the unfunded liability.
- REP. HEINERT said that's true assuming that all new employees are enrolled into the Defined Contribution Plan, that those people wouldn't be paying the 2.2%; what would that do to the Defined Benefits Plan, if in fact, their 2.2% was going into the Defined Benefits Plan to pay that unfunded liability. MR. SCHNEIDER said that that would continue, but it wouldn't solve our problem because the 2.2% is not enough money to pay the unfunded liability. What they need is the 1.64% which is the difference between the normal rate and the contribution rates and the 1.58% which the actuary says they need to pay off the unfunded liability. If you put \$541M today into PERS, you would pay off the unfunded liability and you could drop the Plan Choice Rate.
- 02:42:28 MR. SCHNEIDER said that he is no longer the Executive Director of MPEA but is continuing as an employee of the MPEA Board specifically for the purposes of legislation and the retirement issue. SEN. TROPILA thanked Mr. Schneider for

the years he has devoted to the public employees of the State of Montana.

02:43:16

TOM BILODEAU, Research Director, MEA/MFT

MR. BILODEAU said that he would like to stress two principles that appeared in the initial NCSL document and reiterate MEA/MFT's concern that these principles be recalled. He said that pensions should be understood as mechanisms to provide financial security in retirement for long term employees. Income replacement for retirees upon retirement is the fundamental purpose of a retirement pension program.

02:51:20

COMMITTEE WORK SESSION

MR. BOHYER discussed the Decision Log Sheet (**EXHIBIT 5**) and suggested that because three members of Committee are absent, to adopt these as tentative principles and guidelines and give the other members an opportunity to reflect on them before adopting them as final principles and guidelines.

PRINCIPLE 1: Pensions should provide financial security in retirement.

SEN. BALES moved to adopt. REP. HEINERT seconded. MOTION PASSED UNANIMOUSLY.

PRINCIPLE 2: Pension funding should be a contemporary obligation.

REP. HEINERT moved to adopt. REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

PRINCIPLE 3: Pension investments should be governed by the Prudent Person Rule.

REP. LENHART moved to adopt the principle to say pension investments should be governed by the Prudent Expert Rule. MOTION PASSED UNANIMOUSLY.

PRINCIPLE 4: Pension benefits should be equitably allocated among beneficiaries.

REP. HEINERT moved to adopt. REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

PRINCIPLE 5: Any increase in benefits should be accompanied by an increase of contributions.

SEN. BALES move to adopt. REP. LENHART seconded.

DISCUSSION

MR. BOHYER said that he would recommend that the Committee consider whether or not this should be a guideline that would implement Principle 2. SEN. BALES said that he would withdraw his motion.

SEN. BALES WITHDREW HIS MOTION TO ADOPT PRINCIPLE 5.

GUIDELINE 1: The legislature should approve all changes of benefits. REP. LENHART moved to adopt, seconded by SEN. BALES. MOTION PASSED UNANIMOUSLY.

GUIDELINE 2: The legislature should approve the funding of the state's retirement systems. REP. HEINERT moved to adopt; REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 3: The legislature should regularly review the management of the state's public retirement systems and the investment of the systems' assets. REP. HEINERT moved to adopt, SEN. BALES seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 4: The legislature should establish a permanent pension review body to analyze the problems of the state's public retirement systems on an ongoing basis and to make recommendations for state legislative action. SEN. BALES moved to adopt, REP. HEINERT seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 5: The legislature should require advance funding of pension benefits to ensure that pension costs are not shifted to future taxpayers. SEN. BALES moved to adopt, REP. LENHART seconded.

DISCUSSION

After some discussion, SEN. BALES withdrew his motion and moved for adoption of Guideline 5 that would say: The legislature should require advance funding of pension benefits to ensure that pension costs are not shifted to future taxpayers, including that any increase in benefits should be accompanied by an increase in contributions.

REP. HEINERT asked if it would it be better if it was a guideline of its own. His concern is that it might get lost in what the Constitution and the existing law already says. REP. SMALL EASTMAN asked if we are going to go with increasing your benefits as well as the contributions, should we make it equitable. She said the 3% as contributions is 1% or 2% and then we will be separating ourselves again, so should we have set the same increase both sides. MR. BOHYER said that if the principle is applied, the pension system will be funded with contemporary sources of money and that pension costs are not

shifted to other taxpayers, it's there.

SEN. BALES said that back to the 2001 and so on, we figured we had the funding so we had the advanced funding just from the good fortune of the investments and proposed that Guideline 5 should perhaps say that any benefit increase must be funded by a corresponding increase in employer and/or employee contributions. SEN. BALES said that this guideline would implement Principle 2 and make it clear as to how to ensure Principle 2, which states pension funding should be a contemporary obligation. This is the method whereby this Committee will ensure that it is a contemporary obligation.

REP. HEINERT said that if he hears what Sen. Bales has said, he has revised his motion to include his latest language and he would second that motion.

Guideline 5: The legislature should require advance funding of pension benefits to ensure that pension costs are not shifted to future taxpayers, including that any increase in pension benefits be accompanied by a corresponding and equal increase in employer and employee contributions. SEN. BALES moved to adopt, REP. HEINERT seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 6: The legislature should require a fiscal note when establishing or amending pension plan benefit provisions. REP. LENHART moved to adopt, SEN. BALES seconded.

DISCUSSION

SEN. BALES said that he would amend Guideline 6 to state that the fiscal note would address whether or not the proposed legislation followed the principles and guidelines as set forth.

GUIDELINE 6: The legislature should require a fiscal note when establishing or amending pension plan benefit provisions, and the fiscal note should include a statement whether or not the proposed legislation followed the principles and guidelines as established under section 5-5-228, MCA. REP. LENHART moved to adopt with proposed amendment, REP. HEINERT seconded. MOTION PASSED UNANIMOUSLY.

The Committee recessed for lunch.

PART 2

00:00:01 SEN. TROPILA reconvened at 1:30 p.m.

GUIDELINE 7: The legislature should ensure that the full, long-term costs of early retirement programs and incentives should be calculated before such a program is adopted in order to allow the legislature to provide for the costs. REP. HEINERT moved to adopt, REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 8: The legislature should ensure that post-retirement adjustments should be independently funded and have a ceiling on the percentage of increase for a single year. REP. LENHART moved to adopt, REP. HEINERT seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 9: The legislature should provide strict guidelines for disability coverage and should provide follow-up periodic screenings of disabled retirees. REP. LENHART moved to adopt, REP. HEINERT seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 10: The legislature should use extreme care in developing health insurance provisions for retired employees and, preferably, should provide for separate accounting and funding from retirement programs. REP. LENHART moved to adopt, SEN. BALES seconded.

SEN. BALES moved for adoption of the concept contained in Guideline 10, but would suggest the guideline state: The legislature should make available but not pay for health insurance for retired employees. Health insurance coverage is not a benefit available through the PERS/TRS. REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 11: The legislature should establish strict fiduciary standards and conflict of interest laws to govern the conduct of trustees as they manage the assets of the retirement system. REP. HEINERT moved to adopt, REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 12: The legislature should move toward requiring annual actuarial reports using uniform actuarial assumptions to evaluate the financial soundness of the state's public retirement systems. SEN. BALES moved to adopt, REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 13: The legislature should provide for reciprocity of benefits for workers who shift jobs within the state and its political subdivisions and

portability for those who shift jobs across state lines. REP. HEINERT moved to adopt. REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 14: The legislature should ensure that pension plan participants are fully informed of plan provisions, including benefits, service and vesting requirements, assets and liabilities, investment performance and risk, actuarial assumptions and data, fiduciary requirements and selection of plan trustees. REP. LENHART moved to adopt; SEN. BALES seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 15: The legislature should support coordination of state and local retirement systems. SEN. BALES moved to adopt, REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 16: The legislature should encourage and support the efforts of state retirement system administrators to comply with the principles of pension system administration established by the Public Pension Coordinating Council. REP. HEINERT moved to adopt, SEN. BALES seconded. MOTION PASSED UNANIMOUSLY.

TAPE 3B

GUIDELINE 17: Postretirement benefit increases should not be indexed. REP. LENHART moved to adopt, SEN. BALES seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 18: An annual postretirement benefit increase should be provided. SEN. BALES moved to adopt, REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 19: One-time, *ad hoc* benefit increases should not be enacted. SEN. BALES moved to adopt, REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 20: Minimum benefit increases should be supported. REP. LENHART moved to adopt, REP. SMALL-EASTMAN seconded. Committee and staff discussion concluded that the language in Guideline 20 was unclear, **REP. LENHART moved to adopt Guideline 20 which should read: Increases in the minimum benefit should be supported.** REP. SMALL-EASTMAN seconded. MOTION FAILED.

GUIDELINE 21: Employees should belong to a retirement plan. SEN. BALES moved to adopt, REP. LENHART seconded. MOTION PASSED

UNANIMOUSLY.

GUIDELINE 22: Local governments should have the option of covering rural firefighters under FURS. REP. LENHART moved to adopt, REP. HEINERT seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 23: Retirement benefit formulas in the public safety retirement plans should be similar. REP. HEINERT moved to adopt, REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 24: Retirement benefit formulas or retirement eligibility criteria should not encourage early retirement. SEN. BALES moved to adopt, REP. HEINERT seconded. MOTION PASSED UNANIMOUSLY.

GUIDELINE 25: If retirees return to work they should be encouraged to return to active retirement plan membership. REP. HEINERT moved to adopt, SEN. BALES seconded. MOTION PASSED UNANIMOUSLY.

TAPE 4A

SEN. BALES proposed an additional guideline, **GUIDELINE 26: The amount by which earned investment income exceeds actuarially projected investment income may not be used to fund a benefit increase.** After some discussion, SEN. BALES said that he will not move it at this point in time.

REP. HEINERT moved a new Guideline 26: Excess investment earnings should be used to maintain a reserve account or a rainy day fund. REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

01:05:17

PUBLIC COMMENT

JIM CAMPBELL, Montana Association of Chiefs of Police and the Montana Police Protective Association, said that at this point in time, the police do not receive credit for shift differential pay, holiday pay, or over time pay where other systems do, and they are addressing this.

SEN. TROPILA requested that Mr. Campbell give the Committee a report on what they have decided after they have their meeting.

01:08:24

REP. LENHART moved to adopt Guidelines 1 through 26 with the exception of Guideline 20, which failed. REP. SMALL-EASTMAN seconded. MOTION PASSED UNANIMOUSLY.

01:08:58

NEXT MEETING DATE

The next meeting will be May 12, 2006.

INSTRUCTION TO THE STAFF

SEN. TROPILA requested that Sen. Squires be at the next meeting because draft legislation will be discussed.

Mr. Bohyer said that Kelly Gebhardt was appointed to replace Sen. Tash on this Committee.

REP. LENHART said that he will not be available for the May 12 meeting. Sen. Tropila said Rep. Lenhart will be excused.

REP. HEINERT requested staff to pass on the Committee's concerns to Sen. Tash.

01:19:16 **REP. HEINERT moved that Mr. Bohyer draft a letter to PERB, with a copy to TRB, and inform them of the Committee's request for numbers to see what would happen if new hires were put into a Defined Contribution Plan and not the Defined Benefit Plan; what would be the burden on employers and the contribution that would be required to keep our current system for our current employees actuarially sound. SEN. BALES and REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.**

01:24:32 **NOMINATION OF NEW CHAIR AND VICE CHAIR**
REP. LENHART nominated SEN. TROPILA as Chair. REP. SMALL-EASTMAN seconded. MOTION CARRIED 4-1 with Sen. Tropila opposed.

REP. SMALL-EASTMAN nominated REP. HEINERT as Vice Chair. REP. LENHART seconded. MOTION PASSED UNANIMOUSLY.

ADJOURNMENT

SEN. TROPILA adjourned the meeting at 3:05 p.m.

CI2196 6165kkxa.