



2024 LEGISLATOR'S GUIDE TO MONTANA'S PUBLIC EMPLOYEE RETIREMENT SYSTEMS



**State Administration and Veterans'
Affairs Interim Committee**

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INTRODUCTION

OVERVIEW

The 2024 Legislator's Guide to Montana's Public Employee Retirement Systems (Guide) is designed to serve as an introductory tool to Montana's public employee retirement systems and related policy issues. The State Administration and Veterans' Affairs Interim Committee (SAVA) has been producing the Guide since 2008 to provide background information, reference material, and context for legislators as they make decisions related to the state's retirement systems.

The Guide contains Montana-specific information, as well as general information about public pensions. The Guide does not provide an exhaustive discussion of the different types of retirement plans or of funding policies and other policy considerations. For more information on these matters, contact legislative staff or the staff of the Montana Public Employee Retirement Administration (MPERA) or the Teachers' Retirement System (TRS).

For specifics about benefit, actuarial, and investment data, please refer to the FY 2024 Green Sheets, which can be found here: <https://archive.legmt.gov/committees/interim/sava/sj-4/>. The Green Sheets are updated annually and provide valuable information about the health of the systems.

For more information about past legislation related to Montana's pension systems, please refer to the 2024 version of "Montana's Public Pensions: An Historical Overview of Funding & Benefit Changes in Montana's Public Employee Retirement Systems", which can be found here: <https://archive.legmt.gov/committees/interim/sava/sj-4/>.

IMPACT TO MONTANA

As of June 30, 2024, the actuarial value of trust fund assets in Montana's nine defined benefit public employee retirement systems is \$17.1 billion and the actuarially accrued liability (AAL) is \$19.9 billion. The unfunded actuarially accrued liability (UAAL) is \$4.6 billion.

There are 58,090 active members enrolled and 48,910 retirees and benefit recipients – just over 9% of the state's population or 1 out of every 11 Montanans. Across the state, there are over 1,200 employers participating in the systems, including local governments, school districts, community colleges, and state agencies.

NOTE ABOUT TERMINOLOGY

Throughout this guide, the terms "retirement system" and "retirement plan" are used interchangeably. Nearly all of the public employee retirement plans are referred to as "systems" in Montana statute. All but one of these systems consists of a single plan. However, one system, the Public Employees' Retirement System (PERS), consists of two different retirement plans: a defined benefit plan and a defined contribution plan. Therefore, with respect to PERS, the term "system" refers to both plans.

For the purposes of this guide, the terms "retirement plan" and "pension plan" are used interchangeably. The actual names of most of the public employee retirement plans include the words "retirement system".

A list of pension acronyms can be found in Appendix A and a glossary of pension terms can be found in Appendix B at the end of this report.

CHAPTER 1: MONTANA'S STATEWIDE PUBLIC EMPLOYEE RETIREMENT SYSTEMS

PURPOSE OF RETIREMENT PLANS

A retirement plan is a vehicle designed to ensure that a person will have an ongoing source of income when the person retires and is no longer working. Because of this, retirement plans require that a person meet certain membership and retirement eligibility criteria. Information about the specific criteria for Montana's plans can be found in Table 10 of the FY 2024 Green Sheets:

<https://archive.legmt.gov/committees/interim/sava/sj-4/>.

MONTANA'S STATEWIDE RETIREMENT SYSTEMS

Nationally, pension 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.

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 System (TRS), was formed in 1937. The state's largest plan, the Public Employees' 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.

Today, there are 11 public employee retirement systems in Montana - nine defined benefit (DB) plans and two defined contribution (DC) plans. A public employee becomes a member of one of the retirement plans on the day the employee is hired. These systems cover nearly all state and local government employees, including teachers and public safety officials. All but one of the systems are cost-sharing plans, meaning both the employers and employees contribute to the plans.

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.

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.

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.

CHAPTER 2: TYPES OF RETIREMENT PLANS

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. Montana has nine DB plans and two DC plans. This chapter provides a high-level summary of DB and DC plans. Information about hybrid plans can be found in Appendix D.

DEFINED BENEFIT (DB) PLANS

- A DB plan is an employer-sponsored retirement plan that provides a specific monthly benefit at retirement.
- Retirees receive set monthly installments rather than a lump sum, and the benefit is guaranteed for the rest of their life.
- 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 investment 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.
- 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. As of March 2020, 76% of public employees participated in a DB plan.
- Nine of Montana's 11 statewide retirement systems are DB plans.

DEFINED CONTRIBUTION (DC) PLANS

- A 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. The employee receives the balance in their account upon retirement.
- 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.
- DC plans typically do not pool assets, and instead, employees have a range of investment options to manage individually.
- 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 only offer a DC plan on a statewide basis for broad employee groups.
- Two of Montana's 11 statewide retirement systems are DC plans.

TYPES OF RETIREMENT PLANS - COMPARISON CHART

ISSUE	DB PLANS	DC PLANS
Philosophical Perspective	<p>Employer Responsibility.</p> <ul style="list-style-type: none"> • Employer is obligated to provide a base retirement benefit. • Contributions are pooled, and debts or gains, usually caused by market fluctuations, are shared by employers in the pool. • Unfunded liabilities are typical. • Reasonable amortization schedule provides financial security. 	<p>Employee Responsibility.</p> <ul style="list-style-type: none"> • Employer responsibility ends with contribution to the plan. • Employee bears investment risks and responsibilities. • No gains or losses to a shared plan, so no unfunded liabilities, no amortization schedule, and no actuarial valuations.
Flexibility	<p>Less.</p> <ul style="list-style-type: none"> • A DB plan usually provides only the option of how the defined benefit is to be paid out (e.g., as a single life annuity, joint and survivor annuity, term certain, etc.) 	<p>More.</p> <ul style="list-style-type: none"> • Depending on design, the plan may allow participants to choose contribution amount, investment options, and form of payout.
Portability	<p>Less.</p> <ul style="list-style-type: none"> • Employer contributions are not made to individual accounts, so if an employee leaves employment before vesting, the employee is usually not eligible for a retirement benefit or to take or transfer employer contributions. 	<p>More.</p> <ul style="list-style-type: none"> • Employer contributions are made to individual accounts. Money in the account may not be accessible until retirement, but the employee can continue to manage the account. • Actual portability depends on the specific provisions of the plan, which may or may not limit transferability.
Investment Risk and Return	<p>Risk Assumed by Employer.</p> <ul style="list-style-type: none"> • To the extent that assumptions or projections differ from actual experience, the pension funds may experience gains or losses. • Pension assets are pooled. • Gains and losses are smoothed over a long-term period. • Risk is therefore minimized. 	<p>Risk Assumed by Employee.</p> <ul style="list-style-type: none"> • Employees may select a risk/return tradeoff to fit personal circumstances.
Who Benefits	<p>Career Employees.</p> <ul style="list-style-type: none"> • Typically, longer-term or older employees benefit most. 	<p>Short-Term Employees.</p> <ul style="list-style-type: none"> • Typically, shorter-term and younger employees benefit most (depending on investment choices and realization of assumptions).
Pension Security/ Longevity Risk	<p>Higher.</p> <ul style="list-style-type: none"> • The benefit amount is guaranteed and can be counted on for a lifetime. 	<p>Lower.</p> <ul style="list-style-type: none"> • The actual benefit amount is not known in advance and a retiree could outlive the benefit.
Administrative Costs	Paid by Plan Sponsors.	Paid by Plan Participants.

CHAPTER 3: BENEFIT CALCULATION

HOW BENEFITS ARE CALCULATED

Nationally, the standard equation for determining an individual's benefit at their retirement is:

$$\text{Years of Service} \times \text{Multiplier (\%)} \times \text{Final Average Salary}$$

In Montana, the years of service, multiplier, and highest or final average salary numbers are all set in statute by the Legislature. Additional details can be found in Table 10 of the FY 2024 Green Sheets:

<https://archive.legmt.gov/committees/interim/sava/sj-4/>.

YEARS OF SERVICE

- In the formula, "years of service" is how many qualifying years of service a public employee has worked for their employer within the plan.
- In Montana, all systems have a minimum years of service requirement for vesting. They also have age and/or years of service requirements for retirement eligibility.

MULTIPLIER

- In the formula, the "multiplier" is used to determine the percentage of the highest or final average salary that will be received as a retirement benefit. Years of service are multiplied using this specific number. That amount becomes a percentage of the highest or final average salary. The result equals the amount ultimately received as a benefit in retirement.
- There is a different multiplier for each of the Montana systems, and some systems have different multipliers for different tiers based on hire date.

HIGHEST/FINAL AVERAGE SALARY

- In the formula, the "highest average salary" or "final average salary" is a reference to the compensation amount that a pension will be based on.
- In most states, the highest or final average salary is based on a set number of consecutive years or months of salary.
- In Montana, each of the retirement systems, except for the Municipal Police Officers' Retirement System (MPORS), uses highest average salary for either 3 years or 5 years, depending on the system and hire date. MPORS uses final average salary (3 years).

SAMPLE EQUATION

As of FY 2023, the Sheriffs' Retirement System (SRS) requires 20 years of service to retire. It uses the highest average salary for 3 years for members hired before July 1, 2011, and 5 years for members hired after July 1, 2011. The average salary for SRS members from FY 2021 - FY 2023 was \$64,083. Using these figures as an example, the benefit calculation for a member of the SRS would be:

$$\begin{aligned} \text{Years of Service} \times \text{Multiplier} \times \text{Highest Average Salary (3years)} &= \text{Annual Benefit} \\ 20 \text{ years} \times 2.5\% \times \$64,083 &= \$32,041 \end{aligned}$$

CHAPTER 4: POST-RETIREMENT BENEFIT INCREASES

COST OF LIVING ADJUSTMENTS

Nationally, periodic adjustments in some form, generally referred to as cost-of-living adjustments (COLAs), are provided on most state and local government pensions. The purpose of a COLA is to offset, to some extent, the effect of inflation on retirement income. State to state, there are considerable variations in the way COLAs are designed, and in many cases, they are determined or affected by other factors, such as the actual rate of inflation or the financial condition of the plan. Approximately three-fourths of state and local-sponsored pension plans provide some form of an automatic COLA, one that does not require specific approval or action by the plan sponsor.

GUARANTEED ANNUAL BENEFIT ADJUSTMENT

In Montana, each of the retirement systems, except the Volunteer Firefighters' Compensation Act (VFCA), offers a version of a COLA, called a guaranteed annual benefit adjustment (GABA). In 1997, the Legislature enacted a 1.5% GABA for all Montana Public Employee Retirement Administration (MPERA) systems except for the VFCA. A 1.5% GABA for the Teachers' Retirement System (TRS) was added in 1999. In 2001, the Legislature increased the GABA for the MPERA systems to 3%. After market losses, the GABA was adjusted in 2007 and 2013 providing variable rates for members hired after a certain date. See Table 11 of the FY 2024 Green Sheets for the current rates: <https://archive.legmt.gov/committees/interim/sava/sj-4/>.

CHAPTER 5: ROLE OF THE LEGISLATURE

ROLE OF THE LEGISLATURE

At the state level, Montana's public employee retirement systems are overseen by the Legislature, governing boards, and the Board of Investments. In addition, the systems are subject to all federal regulations and reporting requirements for public pensions. This chapter contains information about the role of the Legislature in overseeing the public employee retirement systems. The next chapter contains information about the role of the governing boards and the Board of Investments. The Legislature is the plan sponsor of the public employee retirement systems and is responsible to the taxpayers. There are specific roles for the full Legislature and individual committees.

STATE ADMINISTRATION AND VETERANS' AFFAIRS INTERIM COMMITTEE

Under section 5-5-228, MCA, the State Administration and Veterans' Affairs Interim Committee (SAVA) has administrative rule review, draft legislation review, program evaluation, and monitoring functions for the public employee retirement plans and shall:

- 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;
- study and evaluate the equity and benefit structure of the state's public employee retirement systems;
- establish principles of sound fiscal and public policy as guidelines;
- as necessary, develop legislation to keep the retirement systems consistent with sound policy principles; and
- publish, for legislators' use, information on the public employee retirement systems that the committee considers will be valuable to legislators when considering retirement legislation.

LEGISLATIVE FINANCE COMMITTEE

The Legislative Finance Committee (LFC) receives annual reports/presentations from MPERA and TRS leadership on the annual actuarial valuation reports on PERS and TRS and their progress towards 100% funding.

LEGISLATIVE AUDIT COMMITTEE

The Legislative Audit Committee (LAC) conducts annual financial compliance audits on the retirement system boards. Recent reports can be found here: <https://archive.legmt.gov/lad/audit-reports/>.

FULL LEGISLATURE

The full Legislature:

- sets the benefit formulas, employee and employer contribution rates, and funding policy in statute;
- receives recommendations from interim committees, retirement boards, and other stakeholders;
- introduces legislation at the request of the retirement boards to ensure the health of the plans; and
- studies the risks and benefits associated with any proposed changes.

Generally, pension-related legislation is referred to the House and Senate State Administration standing committees. This legislation typically also has hearings in the House Appropriations and Senate Finance and Claims committees.

LEGISLATIVE OPTIONS

The Legislature may enact legislation to revise the following aspects of a retirement plan and its funding going forward: (1) contribution amounts; (2) benefit amounts; (3) plan design; and (4) certain investment criteria. Additional information on policy considerations for legislators can be found in chapter 11 of this guide.

Legislative changes in each of these areas have fiscal and policy implications and involve pros and cons. If the Legislature believes that the risk of adverse experience is too high, or the actuarial assumptions are too optimistic (i.e. the assumed rate of return is too high), the Legislature may choose to fund the system based on a scenario in which the plan's experience is more adverse than the assumptions (i.e. a lower rate of return assumption). This will help mitigate the potential financial consequences if adverse scenarios – such as a market crash – come to pass. However, it will also require higher contributions.

The challenge for legislators is how best to balance potential risks of adverse future experience with the policy goal of keeping pension funding obligations contemporary. Keeping pension funding obligations contemporary means trying to ensure future generations are not saddled with past liabilities and that current employees and employers/taxpayers are not required to pay more than the actual cost of their benefits. Because estimating costs requires actuarial assumptions, the risks and potential consequences of actuarial losses will always be part of this equation.

FISCAL IMPACT

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. Any reform of the DB plans requires careful actuarial analysis and consideration of how to continue to pay for the DB plans' 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 and their actuaries, 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. To provide legislators and others with information necessary to make an informed assessment, 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 include the following:

- 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?

CHAPTER 6: PENSION OVERSIGHT

GOVERNING BOARDS

Each plan's governing board members are the plan's responsible fiduciaries, meaning they must act in the best interest of plan members and their beneficiaries.

Nine of Montana's retirement plans (eight DB & one DC) are governed by the Public Employees' Retirement Board (PER Board), a seven-member board, appointed by the Governor. The PER Board oversees the Montana Public Employee Retirement Administration (MPERA), including the hiring of the agency's executive director.

The Teachers' Retirement System (TRS) is governed by the Teachers' Retirement System Board (TRS Board), a six-member board, appointed by the Governor. The TRS Board oversees TRS, including the hiring of the agency's executive director.

MPERA and TRS are responsible for collecting member and employer contributions, calculating benefits, and paying out benefits. They ensure consistency with all federal regulations and reporting requirements. Working with their boards, they hire actuaries to conduct annual actuarial valuations and regular experience studies of the systems. The executive directors provide regular reports to legislative committees and provide recommendations regarding legislation to maintain the health of the plans.

INVESTMENT MANAGEMENT

For the MPERA and TRS DB plans, the 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. The Board of Investments is comprised of nine voting members appointed by the Governor.

Per Article VIII, Section 13 of the Montana Constitution, the BOI is responsible for investing the pooled pension trust funds. They invest using the Prudent Expert Rule and must act in the best interest of the beneficiaries of the funds managed. The board approves the asset allocations and investment policies, and they diversify the holdings to minimize risk while maximizing returns.

PRUDENT EXPERT RULE

The Prudent Expert Rule is a regulatory measure in the federal Employee Retirement Income Security Act (ERISA) that requires fiduciaries to manage pension and profit-sharing portfolios with care, skill, prudence, and diligence. The rule is found in section 404(a)(1)(B) of ERISA and is an updated version of the prudent man rule. It states that fiduciaries must act with the same level of care as a prudent person who is familiar with similar matters and is acting in a similar capacity.

CHAPTER 7: FUNDING SOURCES

FUNDING SOURCES

In Montana, there are four main sources of funding for the retirement systems:

- member/employee contributions;
- employer contributions;
- investment income; and
- statutory and OTO appropriations*.

MEMBER & EMPLOYER CONTRIBUTIONS

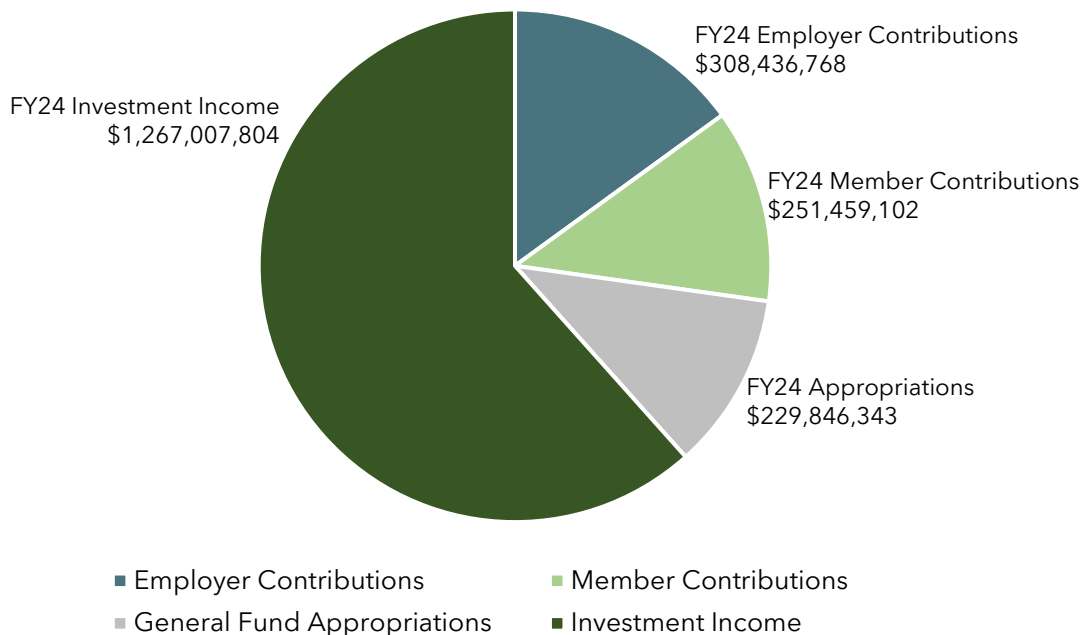
As tax-qualified plans, contributions to Montana's public employee retirement plans are made on a pre-tax basis each pay period. Employee contributions, which are a percentage of the employee's compensation, are withheld from the employee's paycheck and paid directly to the pension plan. Employer contributions are also made directly to the retirement plan each pay period. Both are set in statute by the Legislature.

INVESTMENT INCOME

Pension assets are pooled and managed by the Board of Investments as part of the state's unified investment program. This is the primary source of funding for the DB plans.

STATUTORY AND OTO APPROPRIATIONS

*As of FY 2024, five of the nine DB systems receive supplemental appropriations from the state general fund through statutory appropriations. The plans are TRS, PERS-DB, MPORS, FURS, and VFCA. The appropriation amounts are set in statute by the Legislature. In addition, the Legislature will sometimes give the systems one-time-only (OTO) appropriations through legislation. Totals for FY 2017-FY 2024 can be found in Table 14 of the FY 2024 Green Sheets: <https://archive.legmt.gov/committees/interim/sava/sj-4/>.



CHAPTER 8: ACTUARIAL VALUATIONS AND EXPERIENCE STUDIES

ACTUARIAL VALUATIONS

The MPERA and TRS Boards contract with actuaries to produce annual actuarial valuations of the retirement systems under their purview. Every annual actuarial valuation report includes a section detailing the plan's actuarial gains and losses over 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.

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

The governing boards for the retirement systems set these assumptions based on the actuary's recommendations.

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.

SMOOTHING GAINS AND LOSSES

The actuaries for Montana's plans smooth investment gains and losses over 4 years. This reduces the impact of market volatility when assessing the long-term fiscal soundness of the pension plan. This in turn allows for a steadier approach to funding decisions.

DETERMINING COSTS

The costs of a DB plan - how much employees and employers need to contribute to the plan to pay for future benefits - are estimated based on actuarial valuations. 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.

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, it is recommended that contributions to DB 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. So, 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.

EXPERIENCE STUDIES

Experience studies examine whether actuarial assumptions should be adjusted to better anticipate actual experience. An experience study examines the actual history and experience of the system and measures the assumptions against the actual history. Assumptions about mortality, disability, investment returns, and others may then be adjusted accordingly. 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.

Montana law requires that regular experience studies be conducted for the statewide public employee retirement plans to compare actual experience with the actuarial assumptions. MPERA and TRS conduct experience studies approximately every 4 years. The most recent experience studies were conducted in the spring of 2021 and can be found here:

- MPERA: https://mpera.mt.gov/docs/actuarial_info/2022/2022ActuarialExperienceStudyCONFIDENTIAL-Final.pdf
- TRS: https://trs.mt.gov/miscellaneous/PdfFiles/Information/expstudies/2021_TRS_expstudy.pdf

CHAPTER 9: PERFORMANCE INDICATORS

PERFORMANCE INDICATORS

In a DB plan, the main performance indicators are the funded ratio, the amortization period, and the actual rate of return (in comparison to the assumed rate). Historical trends for these indicators can be found in the FY 2024 Green Sheets: <https://archive.legmt.gov/committees/interim/sava/sj-4/>.

FUNDED RATIO

The funded ratio is the value of a pension plan's assets divided by its liabilities (%). Current assets include the value of all the trust fund's investments. Current liabilities include the value of all accrued benefit obligations. If a DB plan has an unfunded actuarial liability, a DB plan's funded ratio will be less than 100%.

AMORTIZATION PERIOD

The amortization period is the amount of time needed to pay off a retirement system's unfunded actuarial accrued liabilities. Montana uses an open amortization policy, so the period is recalculated each year. Montana's constitution requires that the systems be actuarially sound. Per statute, this means that Montana's systems should amortize in 30 years or less.

INVESTMENT RATE OF RETURN (ACTUAL V. ASSUMED)

Because investment income is the primary source of funding for any retirement plan, the investment return assumption is the most significant assumption used when estimating costs. 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. The assumed rate of return is evaluated every 4 years through experience studies and changed as needed by the governing boards.

CHAPTER 10: POLICY CONSIDERATIONS

POLICY CONSIDERATION FOR LEGISLATORS

Chapter 5 includes information about the role of the Legislature related to pensions. This chapter includes more information about the policy considerations facing legislators when reviewing legislation related to the pension systems.

FUNDING OPTIONS

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

- **Increase Contributions to Sufficiently Fund the Enhancement.** It is generally considered good funding policy that contributions should be sufficient to fund both the normal cost of the benefit enhancement and to amortize in 30 years or less. Legislators may want to consider that raising employer contributions in a retirement system places an additional burden on the employer's budgets and that increased employer contribution requirements for local governments may be considered unfunded mandates.
- **Extend the Amortization Schedule.** If contributions are not increased to cover the costs of enhancing benefits, the system's unfunded liability will increase. A system's unfunded liabilities may be refinanced by extending the amortization schedule. Policymakers asked to extend the amortization period should consider sound policy principles to determine how far the amortization period may be extended before the system is no longer responsibly funded.
- **Apply the Enhancement to New Hires Only.** Applying a benefit enhancement only to new hires will help control costs because no debt for past service is created. This results in a tiered system in which members of the same plan will receive different benefits, which may cause calls for equalized benefits.

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. This does create a tiered benefit structure and results in different treatment of members within the same retirement system, which can cause pressure to equalize benefits.

RATCHET EFFECT

Another policy consideration involves what is termed the "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. Although the Legislature has reduced benefits of future employees, equity and fairness arguments have resulted in bills passed by the Legislature to reinstate the higher benefits for all employees. As mentioned above, this creates a past-service liability and costs that may be beyond what would have been the costs if the benefit had never been reduced.

BENEFIT SWAPS

Benefit-for-benefit "swaps" can sometimes be designed and are legal, provided that the new benefit is of equal or greater value than the old benefit. Such swaps were used to help fund a portion of the costs of the 1.5% GABA granted to certain plans by the Legislature in 1997.

LEAPFROG EFFECT

Another policy consideration may arise if the Legislature passes a benefit enhancement in one system, but not in the other similar systems. If a benefit is increased for members of one system during a legislative session, the Legislature is likely to see a bill to grant that benefit enhancement, or a better benefit, in the other systems as well. This is often referred to as 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. To help prevent leapfrogging, legislators may want to ask proponents of benefits enhancements this question: "If the proposed benefit enhancement is appropriate for members of this system, is it appropriate and should it be granted for members of other systems?"

FIXING FUNDING SHORTFALLS

To address funding shortfalls, legislative options are limited to increasing contributions and reducing benefits. 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.

APPENDIX A: PENSION ACRONYMS

- **457:** Deferred Compensation (457) Plan
- **AAL:** Actuarially Accrued Liability
- **ADEC:** Actuarially Determined Employer Contribution
- **ARC:** Annual Required Contribution
- **ASOP:** Actuarial Standard 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

APPENDIX B: PENSION 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 contributions 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 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.
- **Actuarially Accrued Liabilities (AAL):** The portion of liabilities that exceed the present value of all benefits payable under a defined benefit retirement plan compared to the present value of future normal costs.
- **Actuarially Determined Employer Contribution (ADEC):** The amount actuarially calculated each year that is required to be contributed by an employer to a pension plan's pool of assets to ensure there will be enough funds to pay promised pension benefits. The contribution rate can be reported either in dollars or a percent of salary. Actuaries determine annually how much should be paid by employers in a given year in order to properly fund a pension plan. This amount is a combination of the employer's share of normal cost plus the unfunded liability amortization payment.
- **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.
- **Additional Contributions:** A member's payments to purchase various types of optional service credit.
- **Annual Required Contribution (ARC):** The 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 approach, the unfunded liability is amortized over a set number of years (e.g., 30 years). Each year the unfunded liability is redetermined, reflecting any gains and losses that have occurred, and amortized in 1 fewer year (e.g., 29 years, 28 years, etc.). Each year the amortization period gets shorter, until it reaches 1 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 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.
- **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 American with Disabilities Act of 1990 (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 employee retirement plans are generally not subject to ERISA.
- **Employer:** The state, its university system, or political subdivisions that contract with the appropriate board to cover their employees under a public employee retirement system.
- **Experience Study:** A regular study of the economic and demographic experience of a retirement system, typically administered every 5 years. The purpose is to assess the reasonability of the actuarial assumptions of a retirement system in order to make judgments about future experience and assumptions.
- **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. When a plan is 100% funded, it means current assets are sufficient to pay 100% of benefits due now, as well as the benefits that active and inactive members have accrued to date.
- **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 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 (e.g., 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. The normal cost rate is the contribution amount necessary, when added to investment income, to pay for benefits earned each year.
- **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 (e.g., 30 years). Each year the unfunded liability is recalculated and amortized over a new set amount of years (e.g., 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.
- **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.
- **Stress Testing:** The process of evaluating how pension systems would respond to a variety of potential scenarios, allowing states to gauge the effects of hypothetical adverse market conditions on their retirement systems.
- **Tax Deferred:** The payment of taxes in the future on income earned in the current period.
- **Termination or Termination of Service:** This 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.

APPENDIX C: FY 2024 MEMBERSHIP & SYSTEM DETAILS

SYSTEM	EMPLOYER TYPES	DESCRIPTION	FY 2024 MEMBERSHIP
Teachers' Retirement System (TRS)	<ul style="list-style-type: none"> School Districts Community Colleges Education Co-ops Counties MUS State Agencies 	<ul style="list-style-type: none"> DB Plan Covers teachers in school districts and some state institutions, excluding the faculty of the Montana University System 	<ul style="list-style-type: none"> Active: 20,138 Retirees: 18,002
Public Employees' Retirement System (PERS)	<ul style="list-style-type: none"> State Agencies MUS Counties Cities Schools & Community Colleges Special Districts Some Smaller Police and Rural Fire Depts 	<ul style="list-style-type: none"> DB Plan (default) DC Plan (optional) Largest of Montana's public employee retirement systems Covers most of the general classified positions in state agencies, legislators, and participating local governments, including school districts Local governments and school districts contract with MPERA to participate in PERS 	<ul style="list-style-type: none"> DB Active: 30,604 DB Retirees: 25,824 DC Contributing Members: 5,531
Sheriffs' Retirement System (SRS)	<ul style="list-style-type: none"> Dept of Justice <ul style="list-style-type: none"> Investigators Counties <ul style="list-style-type: none"> Sheriffs Deputies Detention Officers 	<ul style="list-style-type: none"> DB plan Covers sheriffs, sheriffs' deputies, certain others employed in the county sheriff's office, and state investigators employed by the Montana Department of Justice 	<ul style="list-style-type: none"> Active: 1,576 Retirees: 898
Municipal Police Officers' Retirement System (MPORS)	<ul style="list-style-type: none"> City Police Departments 	<ul style="list-style-type: none"> DB plan Covers police officers employed by participating cities, towns, and municipalities 	<ul style="list-style-type: none"> Active: 886 Retirees: 958
Game Wardens' and Peace Officers' Retirement System (GWPORS)	<ul style="list-style-type: none"> Dept. of FWP <ul style="list-style-type: none"> Game Wardens Dept. of Corrections <ul style="list-style-type: none"> Security Guards Probation/Parole MUS <ul style="list-style-type: none"> Campus Security 	<ul style="list-style-type: none"> DB Plan Covers game wardens employed by the state and specified state law enforcement positions, including campus security officers and security guards and probation and parole officers under the Department of Corrections 	<ul style="list-style-type: none"> Active: 1,045 Retirees: 527

Firefighters' Unified Retirement System (FURS)	<ul style="list-style-type: none"> City Fire Departments 	<ul style="list-style-type: none"> DB Plan Covers paid firefighters employed by participating cities, towns, and municipalities 	<ul style="list-style-type: none"> Active: 833 Retirees: 712
Highway Patrol Officers' Retirement System (HPORS)	<ul style="list-style-type: none"> Dept. of Justice <ul style="list-style-type: none"> Highway Patrol Officers Supervisors 	<ul style="list-style-type: none"> DB Plan Covers state highway patrol officers 	<ul style="list-style-type: none"> Active: 225 Retirees: 375
Judges' Retirement System (JRS)	<ul style="list-style-type: none"> Judicial Branch <ul style="list-style-type: none"> Justices/Judges Supreme Court District Courts Water Court 	<ul style="list-style-type: none"> DB Plan Covers district court judges, the supreme court justices, the chief water judge, and the associate water judge employed by the state judicial branch 	<ul style="list-style-type: none"> Active: 60 Retirees: 75
Volunteer Firefighters' Compensation Act (VFCA)	<ul style="list-style-type: none"> Fire Companies as defined in 19-17-109, MCA 	<ul style="list-style-type: none"> DB Plan Covers the volunteer (uncompensated) firefighters of qualifying volunteer fire companies organized in unincorporated areas 	<ul style="list-style-type: none"> Active: 2,723 Retirees: 1,539
Montana University System Retirement Program (MUS-RP)	<ul style="list-style-type: none"> Montana University System 	<ul style="list-style-type: none"> DC Plan Covers faculty and administrators of state-funded higher education institutions 	<ul style="list-style-type: none"> Active: 4,271 Non-Contributing Members (retired, inactive, etc.) - 11,225

APPENDIX D: HYBRID PLANS

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. Core elements of all hybrid plans include mandatory participation, shared financing and risk among employers and employees, pooled assets, and required lifetime benefit payouts.

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. Eleven states offer combination hybrid plans, either optional or compulsory.

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. Five states offer cash balance hybrid plans: California, Kansas, Kentucky, Nebraska, and Texas.

APPENDIX E: INCOME NEEDED & SOCIAL SECURITY

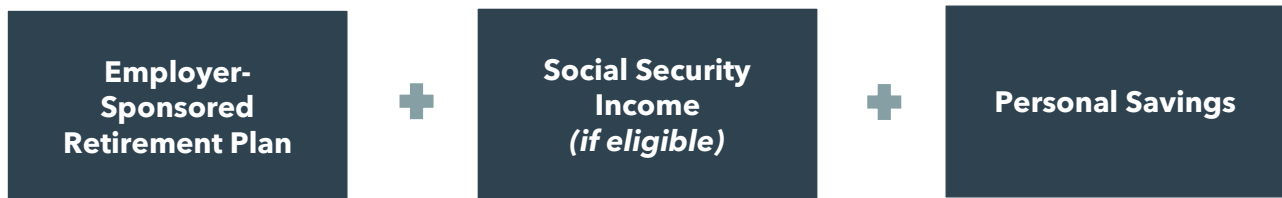
INCOME NEEDED

A familiar metric used by financial planners to help calculate how much income a person will need to live comfortably in retirement is the income replacement ratio—retirement income expressed as a percentage of pre-retirement income.

An individual's ideal income replacement ratio may be higher or lower depending on the individual's pre-retirement salary. For example, a lower-income worker spends a larger proportion of their income on housing, food, and transportation, so they will need a higher income replacement ratio than an average or higher-income worker. Another consideration is that less income may be needed in retirement because certain costs are lower. For example, income taxes will be lower, a family may no longer have expenses related to raising children, and a house mortgage and car loan will be lower or fully paid off. Thus, how much income a retiree needs will vary from household to household.

Keeping in mind there is not a one-size-fits-all target income replacement ratio, studies have concluded that middle-class families need between 65 and 75 percent income replacement ratio to maintain their lifestyle in retirement, and some experts advise a 70 to 80 percent income replacement ratio.

To achieve an adequate income replacement ratio, a person may need to rely on more than one vehicle for retirement savings. Financial advisers often refer to financial security in retirement as resting on a three-legged stool consisting of an employer-sponsored retirement plan, Social Security income (*if eligible*), and personal savings.



SOCIAL SECURITY

The 1935 Social Security Act did not originally allow state and local government employees – including public safety employees such as police officers and firefighters – to participate in Social Security. In 1950, the Act was amended to make coverage optional for certain state and local government employees, but this 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. Today, many police officers and firefighters are still not covered by social security. Instead, their employers take the money they would have paid in social security taxes and put it towards the employees' pension funds.

For information about which of Montana's pension systems are covered by social security, please refer to Table 10 of the FY 2024 Green Sheets: <https://archive.legmt.gov/committees/interim/sava/sj-4/>.

APPENDIX F: LEGISLATION IMPACTING MONTANA'S PUBLIC EMPLOYEE SYSTEMS (1997-2023)

1997 Regular Session

- **HB 170** - Establishes Guaranteed Annual Benefit Adjustments (GABA) for the MPERA pension systems.
- **HB 90** - Calls for an interim study of public pension systems and the development of a defined contribution plan within PERS.

1999 Regular Session

- **HB 72** - Establishes GABA for TRS.
- **HB 79** - Creates the Defined Contribution plan within PERS.

2001 Regular Session

- **HB 294** - Increases GABA amount for MPERA systems and TRS (with conditions for TRS).
- **HB 472** - Transfers Peace Officers from PERS to GWPORS.

2003 Regular Session

- No significant legislation related to public pension systems.

2005 Regular Session

- **HB 102** - Changes appropriation source and schedule for HPORS.
- **SB 370** - Adds Detention Officers to SRS.

2005 Special Session

- **HB 1** - Provides infusion of funds to TRS and PERS-DB.

2007 Regular Session

- **HB 63** - Increases employer contributions and adds \$50M cash infusion to TRS.
- **HB 131** - Decreases GABA for new hires and increases employer contributions for MPERA systems.
- **HJ 59** - Calls for a study of public retirement systems and the creation of the Legislator's Guide to Montana's Public Retirement Systems.

2007 Special Session

- No legislation related to public pension systems.

2009 Regular Session

- **HB 659** - Calls for the SAVA Committee to examine the public pension systems and provide funding and benefit change recommendations to the next Legislature.

2011 Regular Session

- **HB 116** - Changes some benefit provisions in TRS to improve actuarial soundness.
- **HB 122** - Reduces benefits and increases contribution rate for new hires in PERS-DB.
- **HB 134** - Reduces benefits and increases contribution rate for new hires in GWPORS.
- **HB 135** - Reduces benefits and increases contribution rate for new hires in SRS.

2013 Regular Session

- **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.

2015 Regular Session

- No significant legislation related to public pension systems.

2017 Regular Session

- **HB 383** - Increases employee and employer contribution rates and increases funding to SRS to improve actuarial soundness.
- **HB 648** - eliminates coal tax appropriation to the PERS-DB trust fund.

2017 Special Session

- No significant legislation related to public pension systems.

2019 Regular Session

- **HJ 39** - Requests that the Legislative Audit Committee prioritize a performance audit to assess the viability and efficiency of combining TRS and MPERA administrative operations.

2021 Regular Session

- **HB 72** - Revises funding of HPORS to improve actuarial soundness.
- **HJ 8** - Calls for a study of public DB systems and recommendations for a long-term strategic approach to funding.
- **SB 175** - Changes the employer contribution rate for JRS to reduce the system's funding surplus.

2023 Regular Session

- **HB 117** - Adjusts provisions for working retirees in TRS
- **HB 569** - Appropriated OTO funds to HPORS, SRS, and GWPORS; moves JRS, HPORS, SRS, and GWPORS to layered amortization policy; changes retirement eligibility criteria for HPORS and SRS
- **SB 18** - Adds benefit policy statement to all pension systems to prohibit the addition of new benefits without funding
- **SJ 4** - Calls for a study of PERS and TRS DB systems and recommendations for a long-term strategic approach to funding

APPENDIX G: SOURCES & RESOURCES

SOURCES

- https://leg.mt.gov/bills/mca/title_0000/article_0080/part_0010/sections_index.html
- https://leg.mt.gov/bills/mca/title_0190/chapters_index.html
- <https://www.dol.gov/general/topic/retirement/typesofplans>
- <https://equable.org/pension-basics-how-pension-benefits-are-calculated/>
- <https://www.nasra.org/cola>
- <https://www.nasra.org/files/Issue%20Briefs/NASRACOLA%20Brief.pdf>
- <https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/Where%20weve%20been%20-%202018%20update.pdf>
- <https://leg.mt.gov/content/Committees/Interim/2021-2022/State-Administration-and-Veterans-Affairs/Studies-Topics/HJ%208/2020-Legislator-Guide-Pensions.pdf>
- FY 2024 MPERA Valuations: <https://mpera.mt.gov/about/annualreports1/valuations/2024Valuations>
- FY 2024 TRS Valuation: https://trs.mt.gov/miscellaneous/PdfFiles/Information/ActuarialValuations/2024_TRSvaluation.pdf

RESOURCES

- FY 24 Green Sheets and 2024 Historical Overview of Funding & Benefit Changes in Montana's Public Employee Retirement Systems: <https://leg.mt.gov/committees/interim/sava/sj-4/>
- [National Association of State Retirement Administrators](#)
- [Pew Charitable Trusts Fiscal 50 Project](#)
- [Montana Public Employee Retirement Administration](#)
- [Montana Teachers' Retirement System](#)
- [SJ 4 Study Page \(2023-2024 Interim\)](#)
- [HJ 8 Study Page \(2021-2022 Interim\)](#)