

LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
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INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the Net Pension Liability, Deferred Outflows, Deferred Inflows, and Pension Expense included in the accompanying Schedule of Pension Amounts of the Highway Patrol Officers' Retirement System as of and for the year ended June 30, 2017, for the purpose of employer financial reporting for fiscal year 2018. In addition, we have audited the related notes to the schedule.

Management's Responsibility for the Schedule

Management, the Public Employees' Retirement Board, and its staff, the Montana Public Employee Retirement Administration (MPERA), is responsible for the preparation and fair presentation of this schedule in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the schedule that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on the specified amounts included on the Schedule of Pension Amounts as of and for the fiscal year ended June 30, 2017. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the specified amounts on the Schedule of Pension Amounts are free from material misstatement. This report does not include the results of our testing of internal control over financial reporting or compliance and other matters; results are addressed through our separately issued financial audits of the Public Employees' Retirement Board.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures on the specified amounts on the Schedule of Pension Amounts. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement on the specified amounts on the Schedule of Pension Amounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to MPERA's preparation and fair presentation of the specified amounts on the Schedule of Pension Amounts in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of MPERA's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by MPERA, as well as evaluating the overall presentation of the specified amounts on the Schedule of Pension Amounts.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the specified total amounts summarized in the table below are presented fairly, in all material respects, on the Schedule of Pension Amounts for the Highway Patrol Officers' Retirement System, as of and for the fiscal year ended June 30, 2017, for the purpose of employer financial reporting for fiscal year 2018, in accordance with accounting principles generally accepted in the United States of America.

Specified Amounts from the Schedule of Pension Amounts of the Highway Patrol Officers' Retirement System for the June 30, 2017 Measurement Date	Schedule Totals
Net Pension Liability	\$78,385,536
Deferred Outflows	(\$8,075,622)
Deferred Inflows	\$298,637
Pension Expense	\$9,106,866

Other Matters

We have audited, in accordance with auditing standards generally accepted in the United States of America, the financial statements of the Public Employees' Retirement Board as of and for the fiscal year ended June 30, 2017, and our report thereon, dated December 20, 2017, expressed an unmodified opinion on those financial statements. The Highway Patrol Officers' Retirement System is one of several retirement systems that are included in the board's financial statements referred to above.

The opinion on the financial statements discussed in the paragraph above contained an emphasis of matter paragraph stating that two retirement systems, including the Highway Patrol Officers' Retirement System, were not actuarially sound at June 30, 2017, as required by the Montana Constitution. The Highway Patrol Officers' Retirement System amortizes in 37 years. The maximum allowable amortization period is 30 years, as defined by state law. Our opinion was not modified with respect to this matter.

Restriction on Use

Our report is intended solely for the information and use of the Public Employees' Retirement Board and its auditor, Montana Public Employees' Retirement Administration management, Highway Patrol Officers' employer and its auditor, and the Montana Legislature. It is not intended to be, and should not be used by anyone other than those specified parties.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

June 18, 2018

Public Employees' Retirement Board (PERB)

A Component Unit of the State of Montana

Highway Patrol Officers' Retirement System (HPORS)

for the Year Ended June 30, 2018

GASB 68 Single Employer Report	
Schedule of Pension Amounts	
	Measurement Date
	6/30/2017
Total Pension Liability	\$ 218,922,225
Plan Fiduciary Net Position	140,536,689
Net Pension Liability	\$ 78,385,536
Deferred Outflows	\$ (8,075,622)
Deferred Inflows	298,637
Net Impact on Statement of Net Position	\$ 70,608,551
Contributions - Employer	\$ 5,782,258
Pension Expense (\$ Amount)	\$ 9,106,866
Pension Expense (% of Covered Payroll)	61.62%
Discount Rate	7.65%

The Notes are an integral part of this schedule

Public Employees' Retirement Board (PERB)

A Component Unit of the State of Montana

Highway Patrol Officers' Retirement System (HPORS)

Notes to the GASB 68 Single Employer Report

June 30, 2018

The Schedule of Pension Amounts provides the required information under GASB Statement 68 for the HPORS Single-Employer Plan (the Plan). The employer should use this information along with the fiscal year 2018 contribution data to prepare financial reports in accordance with GASB Statement 68.

GASB Statement 68 allows a measurement date of up to 12 months before the employer's fiscal year-end. The information provided with this report are for employers who are using a June 30, 2017 measurement date for their 2018 reporting.

As allowed by GASB Statement 68, the basis for the total pension liability as of June 30, 2017, was determined by taking the results of the June 30, 2016 actuarial valuation and applying standard roll forward procedures. The roll forward procedure uses a calculation that adds the annual normal cost (also called the service cost), subtracts the actual benefit payments and refunds for the plan year, and then applies the expected investment rate of return for the year. The update procedures are in conformity with Actuarial Standards of Practice issued by the Actuarial Standards Board.

Under the direction and oversight of the Public Employees' Retirement Board (PERB), Cavanaugh Macdonald Consulting LLC prepared the GASB 68 Report and calculated the total pension liability; however, responsibility for the data remains with the Montana Public Employee Retirement Administration (MPERA) management, staff of the PERB. The Schedule of Pension Amounts schedule was extracted from the GASB 68 Report.

The financial statements of the PERB *Comprehensive Annual Financial Report* (CAFR) and the GASB 68 Report disclose the Plan's fiduciary net position. Both reports are available on the MPERA website.

Assumptions

The calculations in the GASB 68 Report used the same facts and assumptions found in the FY2017 HPORS Actuary Valuation report. The Summary of Results for the pension plan which includes financial statement information and membership information; Actuarial Procedures and Methods; and Summary of Benefit Provisions are contained in the report.

Contributions

State law defines contributions to the Plan as a percentage of the salary for the employer and the State of Montana. The Plan's actuarial assumptions reflect the current demographics along with the expected long-term contribution effort to the Plan.

No Special Funding

A special funding situation does not exist. The Plan receives contributions from the State of Montana that are *not* recognized as special funding but rather as employer contributions since the State of Montana is the only employer for HPORS.

Schedule of Pension Amounts

The schedule on page 1 provides the total pension liability, the plan fiduciary net position, the net pension liability and the actual contributions for the measurement date. The State of Montana, as the employer, is required to record a liability equal to the net pension liability; the deferred outflows and deferred inflows; total pension expense; and employer contributions.

Deferred Outflows and Deferred Inflows are presented in the schedule on page 1. Since the amortization of certain expense items are over closed periods each year, the deferred portions of these items must be tracked annually. If they increased pension expense, they are labeled deferred outflows. If the amounts reduced pension expense, they are labeled deferred inflows. The amortization of amounts are calculated on a level dollar basis, with no interest included in the deferred amounts. The deferred outflows are not inclusive of the employer contributions subsequent to the measurement date. The employer must obtain and enter this information for their FY2018 reporting.

Gains, Losses and Assumption Changes

The experience gains or losses are the portion of current year changes in total pension liability due to actual versus expected experience for the year. The portion to recognize in the current year was determined by spreading the total change, including any assumption change impacts, over the average expected remaining service life of the entire Plan membership. The average expected remaining service life was estimated at four years. Investment gains and losses are recognized over five years.

For FY2018 reporting, there was a total actuarial experience loss. This total loss is a result of a loss in the financial experience and changes in actuarial assumptions and methods, along with a gain in the benefit changes. Detailed below are the benefit, contribution, assumption and method changes for FY2018 reporting.

The benefit changes were:

- Effective July 1, 2017, the interest rate credited to member accounts increased from 0.25% to 0.77%.
- Working Retiree Limitations apply to retirement system members who return on or after July 1, 2017 to covered employment in the system from which they retired.
- Second Retirement Benefit applies to retirement system members who return on or after July 1, 2017 to active service covered by the system from which they retired and who accrue at least 5 years of service credit before terminating service again.
- Effective July 1, 2017, lump sum payouts in all systems are limited to the member's accumulated contributions rather than the present value of the member's benefit.

There have been no contribution changes since the previous valuation.

Since the June 30, 2016 valuation, the PERB adopted the recommendations made in the experience study for the six-year period ending June 30, 2016.

The assumption changes outlined below, effective July 1, 2017, were used in the June 30, 2017 actuarial valuation.

- Lowered interest rate from 7.75% to 7.65%.
- Lowered the inflation rate from 3.00% to 2.75%.
- Updated non-disabled mortality to the RP-2000 Combined Employee and Annuitant Mortality Table projected to 2020 using scale BB, males set back 1 year.
- Increased the rates of withdrawal.
- Lowered the merit component of the total salary increase.
- Lowered the wage base component of the total salary increase from 4.00% to 3.50%.
- Increased the administrative expense load from 0.23% to 0.30%.

The method changes outlined below, effective July 1, 2017, were used in the June 30, 2017 actuarial valuation:

- Administrative expenses are recognized by an additional amount added to the normal cost contribution rate for the System. This amount varies from year to year based on the prior year's actual administrative expenses.
- To be consistent with the wage base growth change, the payroll growth assumption for amortization as a level percent of pay was reduced from 4.00% to 3.50%.

Employer Notes and Disclosures

As required by GASB Statement 68, the information on page 1 is for the employer's use in their notes and required supplementary information disclosures. The Schedule of Pension Amounts discloses the Total Pension Liability for June 30, 2017; Plan Fiduciary Net Position; Net Pension Liability; Deferred Outflows and Deferred Inflows; and Net Impact on the Statement of Net Position. Other information provided includes the Employer Contributions; Pension Expense; Pension Expense as a Percent of Covered Payroll; and the Discount rate.