BUCK

February 29, 2020

Ms. Kathy Lea
Chief Pension Officer/Deputy Director
Division of Retirement and Benefits
State of Alaska
P.O. Box 110203
Juneau, AK 99811-0203

RE: Fiscal Note for HB 79 Version G

Dear Kathy:

As requested, we are providing a fiscal note analysis for HB 79 Version G ("HB 79G").

HB 79G is a proposed bill dealing with (i) the potential transfer of Peace Officer/Firefighter (P/F) members from the State of Alaska Public Employees' Retirement System Defined Contribution Retirement Plan (PERS DCR) to the Public Employees' Retirement System defined benefit plan (PERS DB), and (ii) all future P/F hires entering PERS DB rather than PERS DCR. In this report, we use "HB 79G members" to refer to P/F members who are affected by HB 79G.

A. Impact of HB 79G on Projected Additional State Contributions for FY22 - FY26

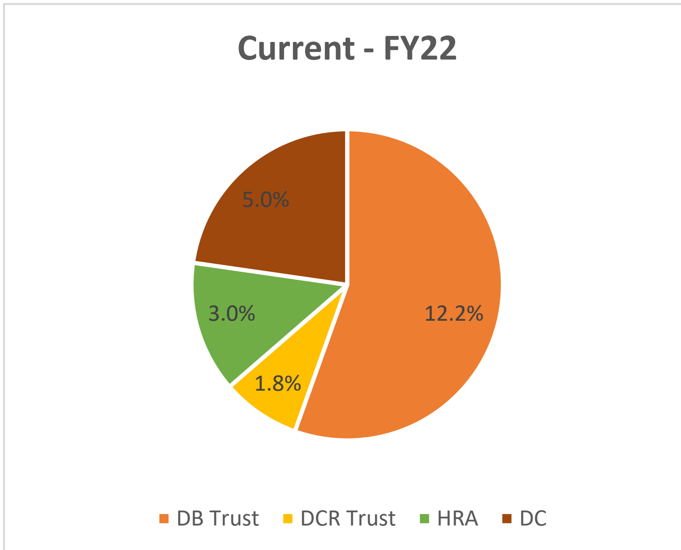
Adverse plan experience (due to poor asset returns and/or unexpected growth in liabilities) or changes to more conservative assumptions will increase the plan's unfunded liabilities, which results in higher Additional State Contributions. The impact of HB 79G on projected Additional State Contributions depends on how large the unfunded liabilities become. If the actuarially determined contribution rate for HB 79G members' pension and healthcare benefits exceeds 9%[1], then HB 79G will lead to larger increases in Additional State Contributions compared to what would have happened without HB 79G. **It is important to recognize that by shifting active P/F members (and all future P/F hires) from DCR to DB, the State will be taking on greater risk of higher contributions in future years. However, this risk is somewhat mitigated as long as the minimum contribution rate to the HB 79G trust (9%) is greater than the actuarially determined contribution rate for HB 79G members.**

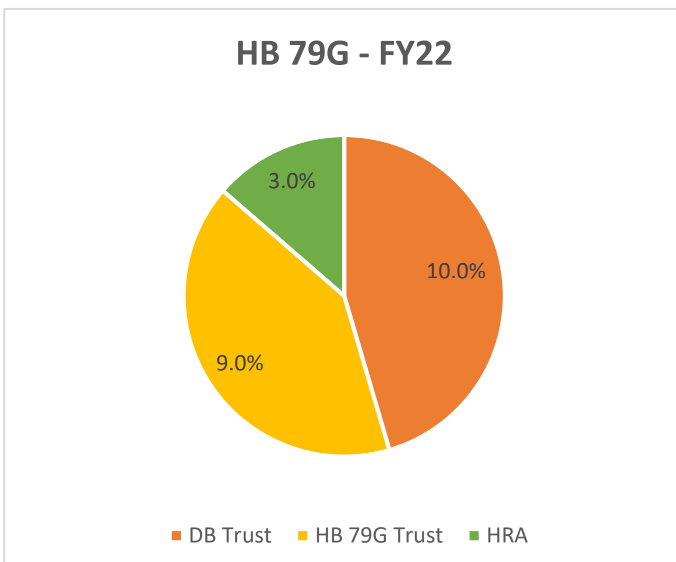
If future experience matches the actuarial assumptions used to value the plan's liabilities, the Additional State Contributions for FY22-FY26 are projected to increase due to HB 79G as shown in the table below. Projected Additional State Contributions beyond FY26 are also expected to increase.

($ millions)	**FY22**	**FY23**	**FY24**	**FY25**	**FY26**	**5-Year Total**
Increase in Additional State Contributions Under HB 79G	$3.5	$3.6	$3.3	$4.0	$4.1	$18.5

[1] The 12% minimum employer contribution rate for HB 79G members less the 3% HRA contribution.

The primary reason for the increase in Additional State Contributions during the 5-year period shown above is illustrated in the pie charts below. These show the distribution of the 22% of pay employer contribution for FY22 for HB 79G members among the various trusts (similar distributions would apply to other years). Because the percentage being deposited to the DB trust decreases (from 12.2% to 10.0%), the Additional State Contribution increases.





B. Summary of HB 79G Benefit Provisions

HB 79G would allow P/F members who are in PERS DCR to make a one-time irrevocable election to transfer to PERS DB within 90 days of the July 1, 2021 effective date of the bill. HB 79G also provides that all future P/F hires will enter PERS DB rather than PERS DCR. The PERS DB benefit provisions that will apply to HB 79G members are summarized below:

- Eligibility for normal retirement benefits is age 60 with 5 years of credited service, or age 55 with 20 years of credited service. The eligibility for healthcare benefits will be the same as the current retiree medical eligibility provisions for P/F members in PERS DCR (i.e., age 65 with 10 years of credited service or any age with 25 years of credited service).
- Member contributions are 8% of pay (and can be increased by the Alaska Retirement Management Board (ARMB) to no more than 10% of pay).
- Average pay used to determine retirement benefits is the 5 consecutive payroll years that yields the highest average.
- The normal retirement benefit is 2% of average pay for the first 10 years of service, and 2.5% of average pay for service over 10 years.
- The Postretirement Pension Adjustment (PRPA) applies, but the Alaska residency-based COLA does not apply, to HB 79G members. The ARMB can reduce the PRPA for HB 79G members if the funded status of the HB 79G trust is less than 90%[2].
- Retiree medical benefits and member premiums are the same as under PERS DCR. Surviving spouses are eligible for medical coverage only if the member had retired or was eligible to retire at the date of death. Election to participate in the retiree medical plan must be made at the later of age 70 ½ or date of retirement. Retired members and spouses must pay the full monthly premium prior to being eligible for Medicare.

C. Employer Contributions Under HB 79G

In accordance with AS Section 39.35.255(a), each employer contributes 22% of pay.

- A new HB 79G trust will be established within PERS and will be used exclusively to fund the pension and healthcare benefits of HB 79G members. Separate HB 79G sub-trusts will be established for pension and healthcare benefits.
- Employers will continue to contribute 3% of pay to the HB 79G members' Health Reimbursement Arrangement (HRA) plan trust in accordance with AS Section 39.30.370.
- Employer contribution rates will be separately determined for the pension and healthcare benefits provided under HB 79G.
- The employer contributions to the HB 79G trust will be the actuarially determined contributions, but not less than 9% of pay (12% minimum employer contribution under AS Section 39.35.255(i) less the 3% HRA contribution). We assumed the 9% minimum employer contribution to the HB 79G trust will be allocated between the pension and healthcare sub-trusts based on the Actuarial Accrued Liability of the HB 79G members' pension and healthcare benefits.
- The excess of the 22% of pay employer contribution over the sum of (i) the employer contribution to the HB 79G trust, and (ii) the 3% HRA contribution will be deposited to the PERS DB trust each year[3].

[2] The funded status of the HB 79G trust is projected to remain above 90% in all years assuming future experience matches the actuarial assumptions used to measure the plan's liabilities.
[3] For purposes of this analysis, the excess contributions made to the PERS DB trust were assumed to be deposited to the pension trust.

D. Assets to be Transferred to the HB 79G Trust

In performing our analysis, we assumed various amounts will be transferred to the HB 79G trust as described below:

- The accumulated employee and employer contributions in each HB 79G member's Defined Contribution (DC) account will be transferred to the HB 79G pension sub-trust to purchase credited service for retirement benefits. The service purchase calculations will be made on an actuarially equivalent basis to be determined by the ARMB[4]. If the amount transferred is insufficient to purchase all of the transferred member's DCR service, the member can create an indebtedness for the shortfall[5]. If the amount to be transferred exceeds the amount needed to purchase all of the member's DCR service, the excess will remain in the member's DC account. If the transferred member terminates before becoming vested in PERS DB, only the transferred employee contributions with interest will be refunded.
- Assets in the PERS DCR retiree medical trust for P/F members will be transferred to the HB 79G healthcare sub-trust. The amount to be transferred equals the increase in the healthcare Actuarial Accrued Liability as of June 30, 2018 for members who elect to transfer.
- Assets in the PERS DCR occupational death & disability trust for P/F members will be transferred to the HB 79G pension sub-trust. The amount to be transferred equals the decrease in the occupational death & disability Actuarial Accrued Liability as of June 30, 2018 for members who elect to transfer.
- The amounts that employers have paid (or will pay) for FY19, FY20 and FY21 to PERS DCR for P/F members' (i) occupational death and disability benefits, (ii) retiree medical benefits, and (iii) DC matching contributions, will be transferred to the HB 79G trust (we assumed these amounts would be deposited to the HB 79G pension sub-trust). The amounts shown below are based on projected payroll.

The asset transfer amounts are summarized below:

- To the HB 79G pension sub-trust
  - $105.6M as of June 30, 2018 for service purchase
  - $2.2M as of June 30, 2018 for decrease in PERS DCR occupational death & disability Actuarial Accrued Liability
  - $10.5M as of June 30, 2019 for FY19 DCR contributions for P/F members
  - $12.0M as of June 30, 2020 for FY20 DCR contributions for P/F members
  - $12.8M as of June 30, 2021 for FY21 DCR contributions for P/F members
- To the HB 79G healthcare sub-trust
  - $16.2M as of June 30, 2018 for increase in PERS DB healthcare Actuarial Accrued Liability

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[4] For purposes of this analysis, the actuarial equivalent basis reflects the assumptions used to determine liabilities for pension benefits in the June 30, 2018 actuarial valuation, except the retirement rates were a blend of 75% of the PERS DCR retirement rates and 25% of the PERS DB retirement rates.
[5] For purposes of this analysis, no employee indebtedness was assumed.

E. Members Assumed to Transfer from PERS DCR to PERS DB

For those who transfer, there will be an additional cost in PERS DB and a reduction in cost in PERS DCR. The net cost impact will depend on (i) how many members transfer and (ii) which members transfer. All results shown in this letter assume 100% of eligible members will elect to transfer from PERS DCR to PERS DB. The actual costs of HB 79G will be based on the actual number and demographics of the members who elect to transfer.

We determined the service purchase amounts based on the Actuarial Accrued Liability of pension benefits in PERS DB (using the June 30, 2018 valuation assumptions and the blended retirement rates described in the next section). For each individual, a comparison was made between their pension Actuarial Accrued Liability and total DC account balance (employee and employer) that was provided to us. If the total DC account balance is equal to or greater than the pension Actuarial Accrued Liability, all of the P/F member's DCR service was credited to PERS DB. If the total DC account balance is less than the pension Actuarial Accrued Liability, only a portion of the P/F member's DCR service was credited to PERS DB[6]. For example, if an individual's total DC account balance was 90% of his/her pension Actuarial Accrued Liability, then 90% of his/her DCR service was credited to PERS DB. The results of this process are described below:

- Of the 1,905 P/F active members in PERS DCR as of June 30, 2018, 1,545 had DC account balances at least equal to their pension Actuarial Accrued Liability, so all of their DCR service was credited to PERS DB. The remaining 360 members had partial DCR service credited to PERS DB.
- On average, approximately 95% of DCR service was credited to PERS DB.
- Approximately $105.6M of the DC account balances at June 30, 2018 were assumed to be transferred to the HB 79G pension sub-trust (this represents approximately 76% of the total DC account balances at June 30, 2018).

F. Additional Notes

The assumptions and methods used in our analysis are the same as those described in the June 30, 2018 actuarial valuation reports, except the retirement assumption used to determine the costs and liabilities for HB 79G participants was a blend of 75% of the PERS DCR retirement assumption and 25% of the PERS DB retirement assumption. For purposes of this analysis, we did not assume any ARMB-directed increases in member contributions under AS Section 39.35.160(e). FY19-FY21 contribution rates that have been adopted by the ARMB were reflected.

The actual FY19 asset return of 6.0% was reflected. Otherwise, we assumed future experience matches the assumptions. The projections assume a stable active population, and the rehire assumption from the June 30, 2018 valuation was assumed to grade to zero uniformly after 20 years (no rehire assumption was applied for HB 79G members).

This study includes only estimated costs due to the net effects on the employer Normal Cost and Unfunded Actuarial Accrued Liability as eligible members transfer from PERS DCR to PERS DB. The study does not include other costs that may be incurred by employers outside of PERS DB or PERS DCR (e.g., potential anti-selection issues that may arise when individuals are presented with a choice between the DB and DCR plans).

The ARMB, staff of the State of Alaska, and HB 79G bill sponsors may use this report for purposes of analyzing the potential cost impact of HB 79G. Use of this report, for any other purpose or by anyone other than the Board, staff of the State of Alaska or HB 79G bill sponsors

[6] For purposes of this analysis, we did not assume any indebtedness would be created for the shortfall.

may not be appropriate and may result in mistaken conclusions because of failure to understand applicable assumptions, methods or inapplicability of the report for that purpose. Because of the risk of misinterpretation of actuarial results, you should ask Buck to review any statement you wish to make on the results contained in this report. Buck will not accept any liability for any such statement made without the review by Buck.

Future actuarial measurements and projections may differ from the current measurements presented in this letter due to such factors as: plan experience different from that anticipated by the economic and demographic assumptions, increases or decreases expected as part of the natural operation of the methodology used for these measurements, and changes in plan provisions or applicable law. An analysis of the potential range of such future differences is beyond the scope of this report.

This report was prepared under our supervision and in accordance with all applicable Actuarial Standards of Practice. David Kershner and Scott Young are Fellows of the Society of Actuaries, Enrolled Actuaries and Members of the American Academy of Actuaries. We meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

If there are any questions, David can be reached at (602) 803-6174 and Scott can be reached at (216) 315-1929.

Respectfully submitted,

David J. Kershner, FSA, EA, MAAA, FCA
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Buck

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Director, Health
Buck