Alaska Retirement Management Board

Senate Finance Subcommittee on Education

August 20, 2013

Alaska Retirement Management Board

- Role of the Alaska Retirement Management Board
- Actuarial Oversight
- ARMB Actions (and Limitations) to Address Unfunded Liability
- Present and Future Course
- Outcomes of Anchorage Stakeholder Workshop

Role of ARMB

Alaska State Pension Investment Board (1992-2005)

1. Responsible for “management and investment of” assets in the retirement funds
2. Liabilities, contribution rates and health care issues addressed by Teachers’ Retirement and Public Employees’ Retirement Boards sited in Department of Administration

Alaska Retirement Management Board (2005-present)

1. Manage/invest assets to meet liabilities & pension obligations of the systems, plan, program, and trusts.
2. Set employer contribution rates
3. Greater duty w/respect to pension liabilities & obligations
4. Recommend to budget-setting and appropriations arms of gov’t, but cannot appropriate or submit a budget

Role of ARMB, contd.

5. Adopt investment policies for each of the Funds; approve investment options for DC plans after consulting with Plan Administrator
6. Approve investment objectives for DB Plans
7. Annual actuarial evaluation to determine assets, accrued liabilities, funding ratios and certify appropriate contribution rate for normal cost and liquidating past service liability
8. Annually report to Governor, legislature, employers valuation of trust fund assets and liabilities and other statistical data to understand system
9. Quarterly report of investment performance to Legislative Budget and Audit
10. Contract for services to execute boards powers and duties

ARMB Powers and Duties

- AS 37.10.071(a)(7): “In making investments under this section, the fiduciary of a state fund shall … perform all acts, not prohibited by this section, whether or not expressly authorized, that the fiduciary considers necessary or proper in administering the assets;”
- 071(c): “In exercising investment, custodial, or depository powers or duties under this section, the fiduciary of a state fund shall apply the prudent investor rule and exercise the fiduciary duty in the sole financial best interest of the fund entrusted to the fiduciary. Among beneficiaries of the fund, the fiduciaries shall treat beneficiaries with impartiality.”

Limited Ability to Impact Unfunded Liability

ARMB Responsibilities:

- Determine asset allocation and investment objectives
- Determine amortization methodology
- Set investment return assumption
- Set employer contribution rates
- Provide input on actuarial assumptions

Limited Ability to Impact Unfunded Liability

ARMB cannot:

- Appropriate funds
- Submit budgets
- Authorize issuance of POBs
- Authorize loans or funding into the retirement system

Actuarial Oversight

- Primary actuary: Responsible for conducting annual actuarial valuation to determine assets, accrued liabilities, funding ratios; certify contribution rate for normal cost and rate for liquidating past service liability; experience analysis performed once every four years
- Review Actuary: Responsible for reviewing and certifying all actuarial assumptions contained in primary actuary valuation and experience analysis before presentation to Board; health cost assumptions reviewed annually
- Auditing Actuary: Responsible for conducting an independent audit of the state's actuary not less than once every four years

Where We Have Been

The Alaska Retirement Management Board has taken actions to address the pension systems' unfunded liability and other issues over the past seven years including:

- ❖ Supported cost-sharing multiple employer system for PERS
- ❖ Supported direct appropriations to PERS and TRS
- ❖ Supported pension obligation bonds
- ❖ Reduced earnings assumption rate to 8%
- ❖ Adopted level-dollar amortization to fund costs sooner rather than later
- ❖ Stakeholder meeting
- ❖ Outreach to Legislature

Where We Have Been

The Alaska Retirement Management Board evaluated 40 potential scenarios in 2011 and supported options which included:

- 25-year or 30-year amortization
- Lump-sum contributions with continued State assistance
- Change to level dollar amortization

Rejected options which included:

- Lump-sum contributions with no further State assistance > 22%
- Cost-shifting from State to municipalities and vice-versa
- Requiring assets outside trust fund be used to set rates
- Extending amortization if significantly higher costs than status quo

Resolution 2013-02

At its February 2013 meeting ARMB passed Resolution 2013-02 requesting:

….that the Alaska Legislature, in addition to state assistance, appropriate in each of the next four sessions the sum of $500 million toward retirement of the unfunded liability of the Alaska Public Employees' Retirement System and Teachers' Retirement System.

Problem Definition

At $11.8 Billion as of June 30, 2012, the unfunded liability of the retirement systems creates growing pressures on the state budget as annual contributions exceed $1 Billion per year under the status quo

Problem Definition: Increasing State Contributions

Growth in Unfunded Liability

- At June 30, 2012

  PERS - $7.4 billion

  TRS - $4.4 billion
- 2005 - $6.9B in 2005 to $11.8B in 2012
- Grew $4.9B in 7 years ($700M / year)

Growth in State Contributions

- 2013 - $608M;
- 2015 = $975M;
- Thereafter > $1B for 8 years; 13 consecutive years > $900M

Status Quo

- FY12 State payroll makes up 61% of total PERS payroll, leading to state paying 81.7% of PERS U/L under SB125
- State pays significant portion of TRS employer contributions
- Employer contribution rate caps: 22% for PERS; 12.56% for TRS
- Retirement System fully funded in 2032 (18 years)

- Interest on PERS/TRS unfunded liability was $889 Million in 2012
- It will take $27 Billion to pay off $12 Billion Liability
- Typically, approx. 70% of pension and health benefits are funded through interest earnings. When the system is underfunded employer contributions must fill the void.

Details of Funding Request

FY 2014-2017 appropriation cycle = $2B infusion

* $250 Million to PERS x 4 years
* $250 Million to TRS x 4 years

Current Actuarial Assumptions Remain in Place

* 8% Earnings Assumption
* Level Dollar Amortization

Details of Funding Request (continued)

Baseline State Assistance PERS and TRS Contributions (2013-2031)	State Assistance after FY14-17 Appropriations $250 Million Each to PERS/TRS
$16.7 Billion	$14.9 Billion

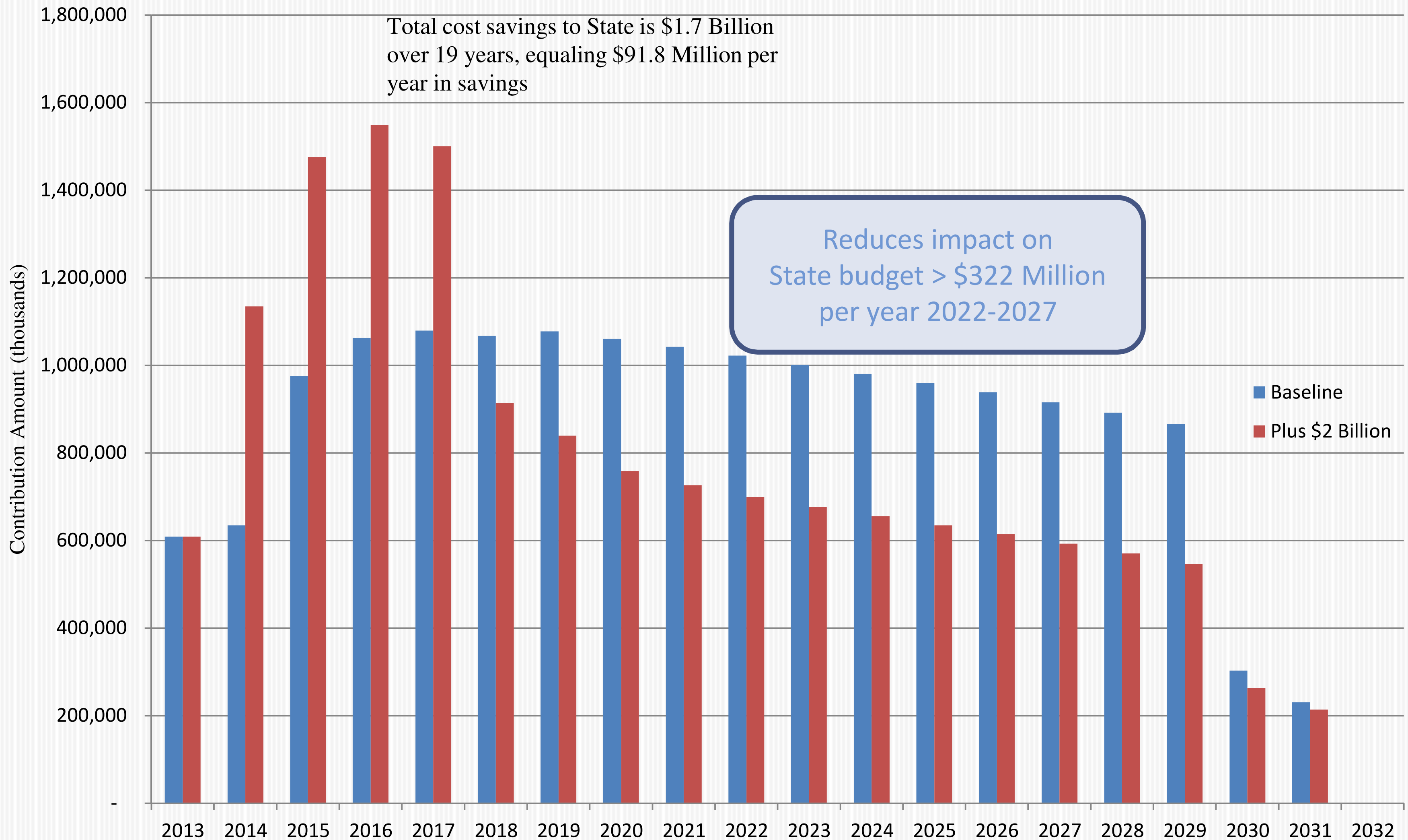
$1.7 Billion Savings in State of Alaska Assistance Contributions

[$91.8 Million Savings Each Year]

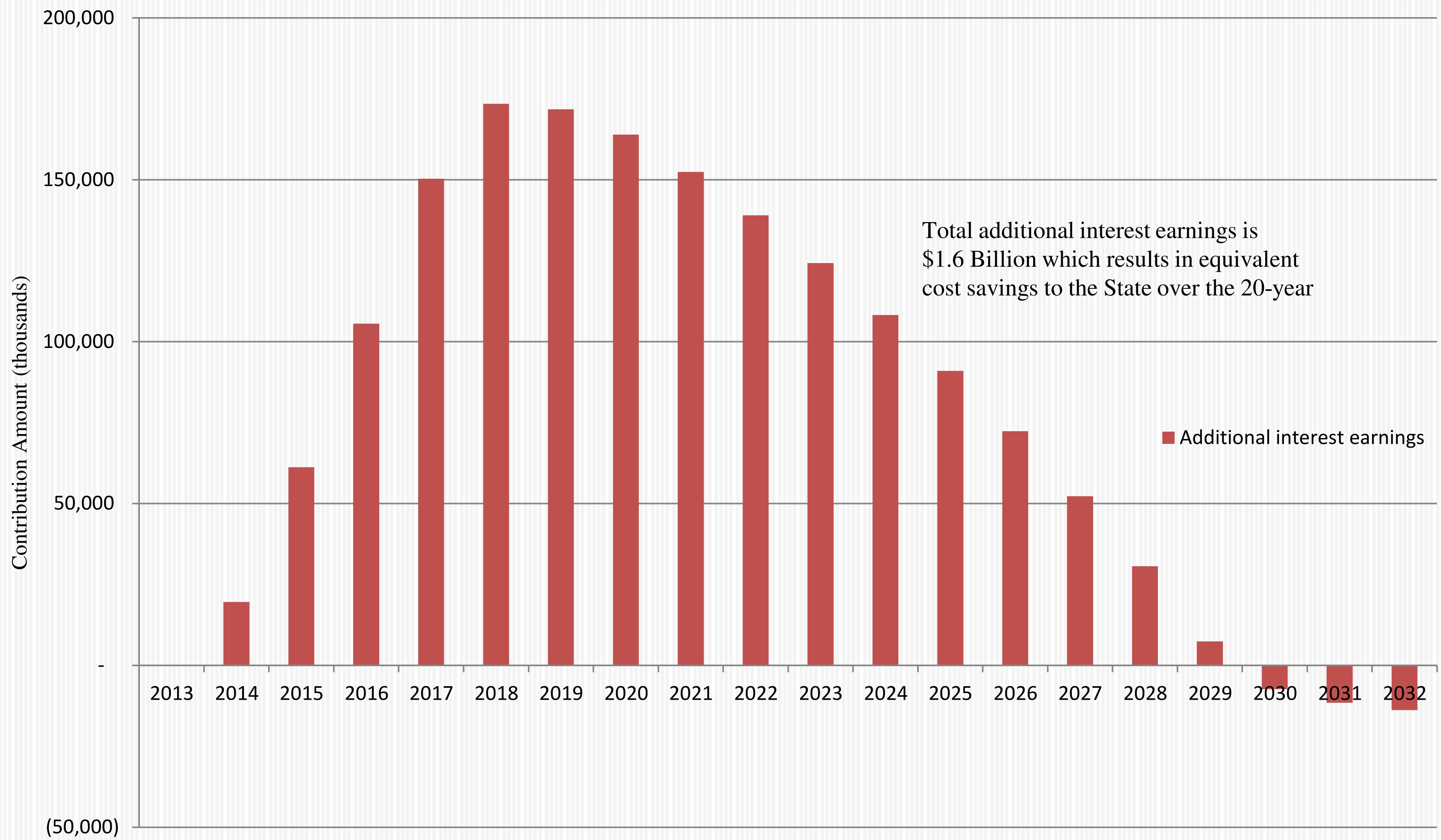
$33 Million Savings in Employer Contributions 2013-2031

[$1.65 Million Savings Each Year – Includes Savings to State as an Employer]

State Assistance: Baseline vs. $2B injection



Additional Fund Earnings with $2B Injection



Annual State Assistance Savings in thousands from $2B Injection* (vs. status quo)

				Level Dollar and 8% return PLUS $250M to PERS and $250M to TRS each year FY14 - FY17			Annual Savings
	Baseline - Level Dollar and 8% return						
	PERS	TRS	PERS + TRS	PERS	TRS	PERS + TRS	
2013	310,528	298,101	608,629	310,528	298,101	608,629	-
2014	319,456	315,053	634,509	569,456	565,053	1,134,509	(500,000)
2015	519,676	455,904	975,580	769,676	705,904	1,475,580	(500,000)
2016	572,439	489,935	1,062,374	815,639	733,165	1,548,804	(486,430)
2017	576,925	502,245	1,079,170	787,294	712,891	1,500,185	(421,015)
2018	563,734	503,650	1,067,384	486,636	426,968	913,604	153,780
2019	566,220	511,074	1,077,294	446,414	392,443	838,857	238,437
2020	549,597	510,979	1,060,576	397,960	360,845	758,805	301,771
2021	530,984	511,071	1,042,055	372,455	354,025	726,480	315,575
2022	511,130	510,919	1,022,049	348,993	350,213	699,206	322,843
2023	490,148	510,769	1,000,917	327,713	349,007	676,720	324,197
2024	469,924	510,255	980,179	307,485	347,931	655,416	324,763
2025	449,483	509,478	958,961	287,253	347,339	634,592	324,369
2026	429,310	508,993	938,303	267,492	347,179	614,671	323,632
2027	407,509	508,033	915,542	245,981	346,594	592,575	322,967
2028	384,751	506,783	891,534	224,501	345,865	570,366	321,168
2029	360,954	505,441	866,395	201,123	344,827	545,950	320,445
2030	10,870	291,874	302,744	-	262,474	262,474	40,270
2031	-	230,333	230,333	-	213,718	213,718	16,615
2032	-	-	-	-	-	-	-
	8,023,638	8,690,890	16,714,528	7,166,599	7,804,542	14,971,141	1,743,387
Savings:	857,039	886,348	1,743,387				

* $500M/year x 4 years

Funding Request (continued)

- For every $1 contributed today, the State saves an *additional* $1 in required future State assistance
- Level Dollar reduces pressure on State budget when oil production is declining and State budget is even more strained
- Cash infusion allows investment earnings to replace employer contributions and state assistance
- Bottom line: Pay now or pay much more later

Stakeholder Meeting

Purpose: *Provide a forum for stakeholders to discuss potential solutions to pay down the retirement systems' unfunded liability and mitigate the impact of increasing retirement system contributions on future state budgets.*

Attendees included: Legislators and/or staff; OMB, DOR, DOA; NEA, RPEA, APEA, Firefighters; AGFOA, AML, AASB

Primary Outcomes

- Borrow from ourselves
  - Mitigates risks of borrowing from capital markets
  - Provides guaranteed return to reserves
  - Prefer to borrow from CBR since SBR earnings are swept into GF
  - State's bond rating not adversely affected if we borrow from ourselves
  - Demonstrates that Alaska has a plan to address U/L
  - Leverages significant reserves without consuming them
- Direct appropriation
  - Prefer a single lump-sum rather than spread over multiple years
- Pension Obligation Bonds as a partial solution

Majority agreed on the need for substantial injection into system now.

ARMB Next Steps

- Respond to Governor's question: What level of up-front contribution into the retirement system, combined with level dollar amortization, would be needed to reduce future state assistance payments from today's levels?
- Outreach/Education to the legislature and other stakeholders
- Research/education issues from stakeholder meeting

Thank You

The Alaska Retirement Management Board thanks the Alaska State Legislature for its commitment to fund the State's retirement system, and for its consistent annual contributions to the Systems.

Thank you also for the opportunity to present this information to you.

APPENDIX

ARMB Role

ARMB powers and duties:

- "AS 37.10.220(a)(2): "after reviewing recommendations from the Department of Revenue, adopt investment policies for each of the funds entrusted to the board."
- 220(a)(3): "determine the appropriate investment objectives for the defined benefit plans.."
- 220(a)(4): "assist in prescribing the policies for the proper operation of the systems and take other actions necessary to carry out the intent and purpose of the systems in accordance with AS 37.10.210 – 37.10.390."
- 220(a)(8): "coordinate with the retirement system administrator to have an annual actuarial evaluation…prepared to determine system assets, accrued liabilities, and funding ratios and to certify to the appropriate budgetary authority of each employer in the system (A) an appropriate contribution rate for normal costs; and (B) an appropriate contribution rate for liquidating any past service liability."

ARMB Role

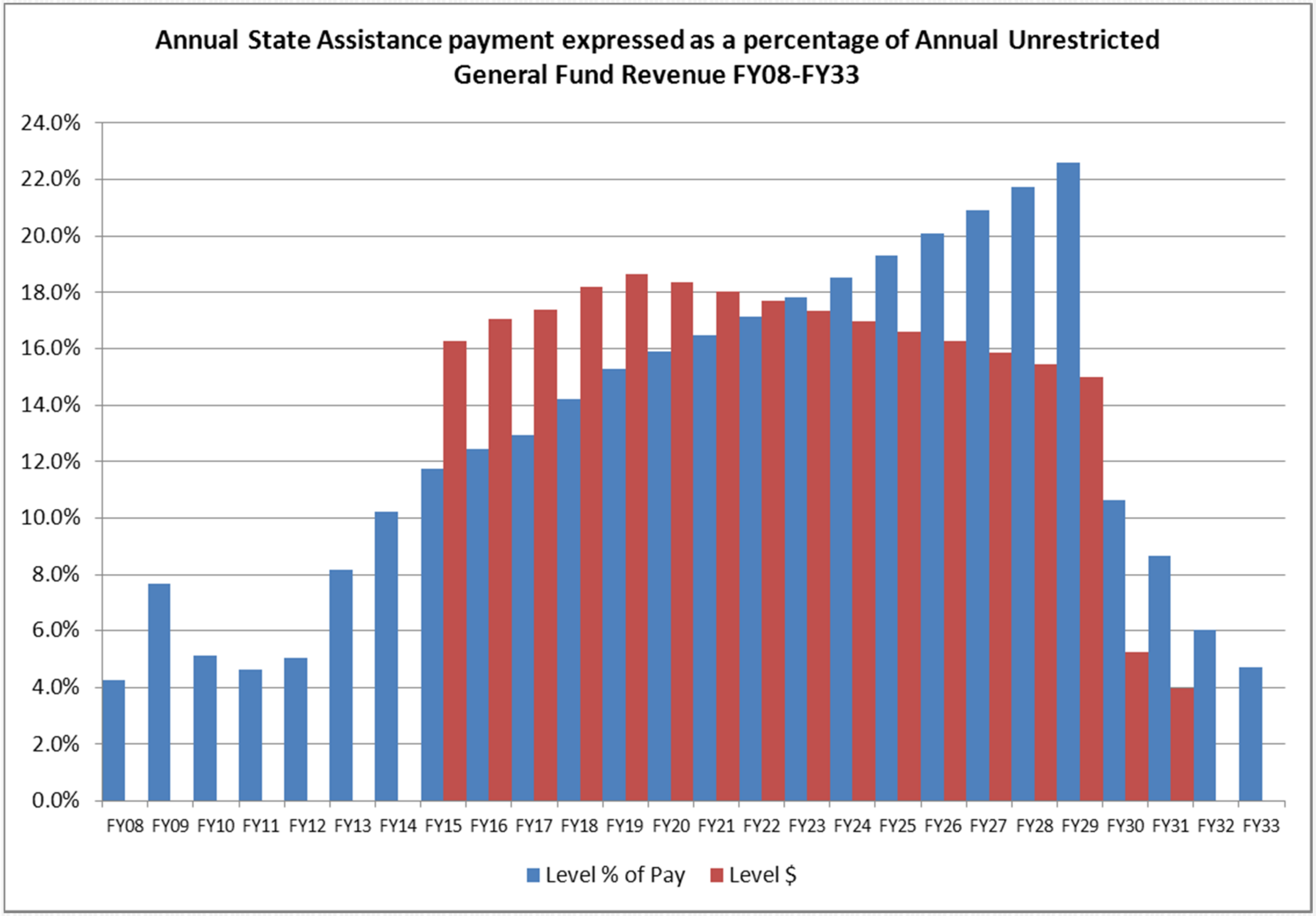
ARMB powers and duties:

- 220(a)(13): "[annually]…report to the governor, the legislature, and the individual employers…on the financial condition of the systems in regard to (A) the valuation of trust fund assets and liabilities….and (G) other statistical data necessary for proper understanding of the financial status of the system."
- 220(a)(14): "Submit quarterly updates of the investment performance reports to the Legislative Budget and Audit Committee."
- 220(b)(3): "contract for other services necessary to execute the board's powers and duties."

Role of Review Actuaries

- AS 37.10.220(a):
- 220(a)(8): Coordinate with the retirement system administrator to have an annual actuarial valuation of each retirement system prepared to determine system assets, accrued liabilities, and funding ratios and to certify to the appropriate budgetary authority of each employer in the system (A) an appropriate contribution rate for normal costs; and (B) an appropriate contribution rate for liquidating any past service liability
- 220(a)(9): Review actuarial assumptions prepared and certified by a member of the American Academy of Actuaries and conduct experience analyses of the retirement systems not less than once every four years, except for health cost assumptions, which shall be reviewed annually; the results of all actuarial assumptions prepared under this paragraph shall be reviewed and certified by a second member of the American Academy of Actuaries before presentation to the board;
- 220(a)(10): Contract for an independent audit of the state's actuary not less than once every four years;
- 220(a)(11): Contract for an independent audit of the state's performance consultant not less than once every four years;
- 220(a)(12): Obtain an external performance review to evaluate the investment policies of each fund entrusted to the board and report the results of the review to the appropriate fund fiduciary;

Why change Level % of Pay to Level Dollar



PERS: 2012 increase in Unfunded Liability

Public Employees' Retirement System

Changes in Unfunded Liability Since Last Year
($ in millions)

Development of Change in Unfunded Liability during FY12		
1. 2011 Unfunded Liability		$6,927
a. Interest on unfunded liability	$554	
b. Normal cost	289	
c. Employee contributions	(113)	
d. Employer contributions	(406)	
e. State relief under SB 125	(243)	
f. Medicare Part D subsidy	(32)	
g. Interest on b., c., d., e., and f.	(8)	
h. Expected change in unfunded liability during FY12		41
2. Expected 2012 Unfunded Liability		$6,968
a. Liability (gains)	$(540)	
b. Assets losses	805	
c. Change in healthcare assumptions	227	
d. Other changes in unfunded liability during FY12		492
3. Actual 2012 Unfunded Liability		$7,460

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PERS: 2012 change in Employer/State Contribution Rate

Public Employees' Retirement System

Peace Officer/Firefighter and Others Combined
Change in Total Employer/State Contribution Rate

Normal cost: 6.82%;
Past service cost: 33.03%
Total Rate: 39.85%

	Pension	Healthcare	Total
1. Last year's total Employer/State contribution rate	16.47%	15.84%	32.31%
2. Change due to:			
• Change in amortization method	4.89%	2.32%	7.21%
• New healthcare assumptions	N/A	0.75%	0.75%
• Effect of two-year delay in the contribution rate	0.25%	(0.04%)	0.21%
• Asset experience	2.40%	0.71%	3.11%
• Salary increases	0.23%	N/A	0.23%
• Demographic experience and other*	(1.00%)	(1.23%)	(2.23%)
• Claims costs	N/A	(1.74%)	(1.74%)
• Total change	6.77%	0.77%	7.54%
3. Total Employer/State contribution rate this year	23.24%	16.61%	39.85%

*Includes data and programming changes.

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TRS: 2012 increase in Unfunded Liability

Teachers' Retirement System

Changes in Unfunded Liability Since Last Year
($ in millions)

Development of Change in Unfunded Liability during FY12		
1. 2011 Unfunded Liability		$4,191
a. Interest on unfunded liability	$335	
b. Normal cost	98	
c. Employee contributions	(52)	
d. Employer contributions	(74)	
e. State relief under SB 125	(235)	
f. Medicare Part D subsidy	(13)	
g. Interest on b., c., d., e., and f.	(7)	
h. Expected change in unfunded liability during FY12		52
2. Expected 2012 Unfunded Liability		$4,243
a. Liability (gains)	$(192)	
b. Assets losses	359	
c. Change in healthcare assumptions	67	
d. Other changes in unfunded liability during FY12		234
3. Actual 2012 Unfunded Liability		$4,477

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TRS: 2012 change in Employer/State Contribution Rate

Teachers' Retirement System

Change in Total Employer/State Contribution Rate

Normal cost: 6.40%;
Past service cost: 59.91%
Total Rate: 66.31%

	Pension	Healthcare	Total
1. Last year's total Employer/State contribution rate	31.40%	18.70%	50.10%
2. Change due to:			
• Change in amortization method	9.52%	3.55%	13.07%
• New healthcare assumptions	N/A	0.63%	0.63%
• Effect of two-year delay in the contribution rate	0.52%	0.19%	0.71%
• Asset experience	3.47%	0.71%	4.18%
• Salary increases	0.00%	N/A	0.00%
• Demographic experience and other*	(0.36%)	(0.29%)	(0.65%)
• Claims costs	N/A	(1.73%)	(1.73%)
• Total change	13.15%	3.06%	16.21%
3. Total Employer/State contribution rate this year	44.55%	21.76%	66.31%

*Includes data and programming changes.

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