

# ALASKA STATE LEGISLATURE

Sen. Fred Dyson, Chair  
Sen. Cathy Giessel, Vice Chair  
Sen. John Coghill  
Sen. Bert Stedman  
Sen. Bill Wielechowski



State Capitol, Room 121  
Juneau AK 99801-1182  
907-465-2199  
Fax: 907-465-3818  
800-342-2199

## Senate State Affairs Committee

### MEMORANDUM

**To:** Committee Members  
**From:** Senator Dyson, Chairman  
**Date:** 4/1/2013  
**Re:** SB 48 Questions to Dept. of Administration with Responses From the Deputy Commissioner (Barnhill)

---

After the committee heard SB 48 at the 3/12/hearing, we sent the following questions to the Department of Administration—the responses from the Deputy Commissioner (Barnhill) follow each question:

1. How much of the debt SB 48 seeks to forgive can be tied to faulty actuarial advice from the actuary the State sued and secured a negotiated settlement from?  
  
A: Interesting question, and based on my involvement in the actuarial malpractice litigation at [the Department of] Law, I have a fairly informed view—though you may disagree with it.

In the Mercer litigation, we were seeking three basic forms of damages: (1) the principal amounts that we should have collected from employers over the time period in question, but didn't because of negligent advice from Mercer; (2) investment earnings on those principal amounts; (3) punitive damages for false reporting.

At oral argument, Judge Collins expressed grave concerns about the validity of our claim for principal amounts that we did not collect from employers. In her view, those were amounts that employers owed regardless of Mercer's negligence, and that if anything, by retaining those funds the employers had the benefit of the use of those funds through to the present. We subsequently settled

the case. The net amount we recovered (\$403mm) equated to the investment earnings that we lost by not having the principal amounts from employers during the time period in question.

**That’s a long way of saying, that in my view, the systems recovered 100% of their actual losses attributable to Mercer’s conduct. The amounts not recovered were and are employer obligations.** (we also did not recover our claim for punitive damages—but that is an amount that is not tied to loss, but an amount intended to punish for outrageous conduct).

I don’t expect everyone to agree with that view, but having been a part of the legal team that handled that case, I feel very comfortable with it.

That being said, the amounts at issue in SB 48 are only indirectly related to actuarial malpractice. The amounts at issue are the difference between 22% of the employer’s current payroll and 22% of the employer’s 2008 payroll. That differential is the product of 2008 legislation (SB 125) that was intended to maintain a certain level of political subdivision participation in paying off the unfunded liability. The unfunded liability has multiple causal factors: (1) negligent incorrect actuarial assumptions regarding health care cost growth; (2) non-negligent but nevertheless incorrect actuarial assumptions regarding investment returns; and (3) changes to multiple actuarial assumptions, including investment return, healthcare cost growth, etc.

2. Regarding policy/legal issues related to municipalities, as long as current Alaska law precludes municipal bankruptcies, do any other debt restructuring options exist for municipalities in Alaska statute?

We’re assuming not, as SB 44 is before the committee—should there be?

The best I can articulate this is, “should/could there be a bankruptcy like mechanism for municipalities to restructure at least the obligations being considered by SB 48? . . . .

A: At this point, we are very uncomfortable recommending bankruptcy as a means for restructuring public pension obligations. Litigation is currently pending in California federal court regarding whether the municipalities of Stockton and San Bernadino can discharge obligations to CalPERS in bankruptcy. Court decisions on this issue should come relatively soon.

There are at least two policy perspectives that we take into consideration here:

**First, protecting the system:** is there a funding mechanism in place that will ensure that all benefits will be paid when due?

Under SB 125, for now, the answer is yes—every year the participating employers and legislature pay the entire actuarially

required contribution to ensure that the unfunded liability will be retired in 25 years. If a municipality were to discharge its public pension obligation in bankruptcy or by some other means, this would not directly impact system funding, because that obligation is simply shifted to the state under SB 125. So from this policy perspective, the system is relatively indifferent to municipal bankruptcy, so long as SB 125 is in place and the legislature continues to appropriate the actuarially required amount.

**But that begs the second policy perspective, which is the importance of sustainable solutions and maintaining appropriate employer participation in the retirement of the unfunded liability.** At what point does shifting costs to the State become unsustainable?

We believe that sustainability, and basic fairness, require robust participation by all PERS employers in retiring the unfunded liability. For that reason, we are reluctant to concede solutions that result in material cost shifting. There is also a view that is reluctant to concede solutions that result in immaterial cost shifting because of the fear of what happens once the door is opened to any cost shifting.

3. How many other communities are on the verge, or headed towards the 25% population decrease as the 3 communities the bill currently addresses?

A: We have that information, and if it hasn't already been provided, we will send separately.

4. [We] [w]ould like Dept. of Admin's perspective on the problem, in general, and specifically, if there are any ideas over there . . . about how to give relief to municipalities that are true victims without extending a benefit to municipalities that might game the system. Senator Stedman identified municipalities that were "gaming" they system as one of the reasons for SB 125.

A: I think some of this is covered in my response to question 2. Another option to consider is to revisit this on an annual basis through the appropriation process. Is it wise to give permanent relief if there is a possibility that one or more of these communities may experience a population rebound at some point in the future?