

MINUTES
SENATE FINANCE COMMITTEE
March 17, 2005
9:15 a.m.

CALL TO ORDER

Co-Chair Green convened the meeting at approximately [9:15:21 AM](#).

PRESENT

Senator Lyda Green, Co-Chair
Senator Gary Wilken, Co-Chair
Senator Con Bunde, Vice Chair
Senator Fred Dyson
Senator Bert Stedman
Senator Lyman Hoffman
Senator Donny Olson

Also Attending: JOELLEN HANRAHAN, Director, Division of Administrative Services, Department of Community and Economic Development; MARC ANTRIM, Commissioner, Department of Corrections; TRACI CARPENTER, Staff to Senator Lyda Green

Attending via Teleconference: There were no teleconference participants.

SUMMARY INFORMATION

SB 46-APPROP: CAPITAL BUDGET

The Committee heard budget overviews from the Department of Commerce, Community and Economic Development and the Department of Corrections. The bill was held in Committee.

SB 141-PUBLIC EMPLOYEE/TEACHER RETIREMENT

The Committee heard from the bill's sponsor and the bill was held in Committee.

#sb46

SENATE BILL NO. 46

"An Act making capital appropriations and appropriations to capitalize funds; and providing for an effective date."

This was the second hearing for this bill in the Senate Finance Committee.

Department of Commerce, Community and Economic Development

Manufacturing Extension Program

\$1,600,000

\$800,000 BLic Rcpts

\$800,000 Fed Rcpts

Reference No.: 40242

Category: Development

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005 - 06/30/2010

One-Time Project

The Federal Manufacturing Extension Program (MEP) will support Alaska's small and medium sized manufacturers throughout the state by providing them access to knowledgeable manufacturing and business specialists throughout the United States. This program contributes to the Department's mission of promoting a healthy economy by developing the business skills of Alaska's small manufacturing companies.

JOHANA HANRAHAN, Director, Division of Administrative Services, Department of Commerce, Community and Economic Development, informed the Committee that this request has been removed from this legislation, and is being advanced in the Supplemental bill legislation.

Alaska Visitors Statistics Program

\$750,000 Gen Fund

Reference No.: 40078

Category: Development

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005-06/30/2010

One-Time Project

Continuation of the Alaska Visitors Statistics Program (AVSP). This Program continues the comprehensive collection and presentation of information on Alaska's visitors. This program contributes to the Department's mission of promoting a healthy economy by assisting the visitor industry in marketing Alaska.

Ms. Hanrahan stated that this continuing program provides demographic, characteristic, and expenditure patterns and opinions of travelers to the State. The information is used to gauge impacts to visitor infrastructures and facilities, to determine investments

in visitor attractions and services and the effect on State lands and other natural resources, and to develop the tourism-marketing program.

Senator Bunde commented that this program must be "a great asset" to commercial enterprises in the visitor industry. Due to the fact that the State is shifting to a policy of user pay, he asked whether an estimate on the project's rate of return to the general fund has been developed.

Ms. Hanrahan responded that data that has been gathered pertaining to the increase in the number of visitors and revenues resulting from promoted venues might address the question. Specific information would be provided.

Senator Bunde stated that the State must seek more support from the industry.

Tourism Promotion
\$530,000 Gen Fund
Reference No.: 40495
Category: Development
Location: Statewide
Election District: Statewide
Estimated Project Dates: 07/01/2005-06/30/2010
One-Time Project
Various tourism marketing projects to promote and increase tourism in Alaska. This request contributes to the Department's mission of promoting a healthy economy by assisting the tourism industry and those businesses benefiting from the tourism industry.

Ms. Hanrahan stated that this project has five different components: to augment national cable network television marketing by increasing the number of weeks of advertising; to expand the number of national cable networks being utilized; to increase the State's online advertising presence on key trip-planning websites; and to enhance the TravelAlaska.com website specifically to include an online forum on the site. Research has indicated that an increasing number of travelers are using Internet websites to plan and research travel options.

Senator Bunde reiterated that the return to the State should be a consideration as "creating jobs is not enough".

Senator Hoffman asked regarding the justification for requesting a one-year rather than an on-going marketing program; specifically whether the one-year request is being proposed to address a lull in

the number of visitors to the State.

Ms. Hanrahan responded that this is considered to be a multi-year project, as the request would provide funds for more than one year. The project would boost tourism.

Senator Hoffman inquired to the amount of the request that would be expended in FY 06.

Ms. Hanrahan replied that this information would be provided.

Co-Chair Green asked that the total FY 06 tourism category funding, to include all fund sources in both the operating and capital budgets, be provided.

Ms. Hanrahan stated that this information would be compiled.

Ms. Hanrahan continued that the request would also promote independent visitor traffic on the Alaska Highway by providing funds to pre-qualified journalists to experience and write about it. Independent travel on the Alaska Highway has been experiencing limited growth. The fifth area that would be addressed with these funds would be to further sales and training missions to promote an Alaska/Asian relationship.

Organization Grants

\$700,000 Gen Fund

Reference No.: 40056

Category: Development

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005 - 06/30/2010

One-Time Project

Grants to unincorporated communities to defray the cost of incorporation. Each unorganized city or borough that incorporates after December 31, 1985 is entitled to an organization grant under AS 29.050.180 -.200. This grant contributes to the Department's mission of promoting a healthy economy and strong communities by assisting communities in achieving maximum self-government.

Ms. Hanrahan stated that this request would provide grants to assist local governments in transitioning to a borough. Potentially the Prince William Sound area, the City of Delta Junction/Delta-Greely area, the Anchor Point area, and others might soon become organized boroughs.

Co-Chair Green asked whether this could be characterized "as just

an anticipation."

Ms. Hanrahan responded that some of the petitions have been filed and others are anticipated. According to Title 29 guidelines, communities that organize are entitled to receive State funding assistance for three years after organization. This funding request would fund the first of three years.

Senator Olson asked for further information regarding the assistance that must be provided to organizing communities.

Ms. Hanrahan responded that a newly organized borough or unified municipality would receive \$300,000 its first year, \$200,000 the second year, and \$100,000 the third year.

Senator Olson understood therefore that \$600,000 would be provided.

Co-Chair Green commented this is the amount specified in State statute.

Ms. Hanrahan concurred.

Community Development Grants

\$14,538,000

\$14,050,000 Fed Rcpts

\$ 488,000 Gen Fund

Reference No.: 38943

Category: Development

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005 - 06/30/2010

On-Going Project

Multiple federally-funded programs, enabling Commerce to provide grants to communities and non-profit organizations for community development. This program contributes to the Department's mission of promoting a healthy economy and strong communities by providing economic growth in the communities it serves.

Ms. Hanrahan informed that this program assists communities with developing flood plains and erosion management programs; grants to assist small communities expand and diversify their economy; and programs that allow Rural communities to construct or remodel multi-use facilities. Communities contribute a match ranging from ten to 25 percent of the cost of such projects. In FY 05 and FY 06, 48 unmapped communities in the Lower Kuskokwim and Bering Straits, Copper Valley, and Southeast areas would receive accelerated infrastructure development grants that would allow them to develop

profile maps. The request would also provide funds to the State's Bulk Fuel Bridge Loan program and funds to mitigate the impact of the Fort Greely Missile Defense development's construction and operation.

Community Block Grants

\$6,115,000

\$6,045,000 Fed Rcpts

\$ 70,000 Gen Fund

Reference No.: 38946

Category: Development

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005 - 06/30/2010

On-Going Project

Multiple federally-funded programs, enabling Commerce to provide grants to communities and non-profits that provide services and/or benefit the low- to moderate- income individuals. This program contributes to the Department's mission of promoting a healthy economy and strong communities by providing economic growth in the communities it serves.

Ms. Hanrahan stated that this long-term on-going program would provide funds to the Rural Alaska Community Action Program (RACAP) for such things as training and educational drug and alcohol abuse programs as well as nutrition grant programs. Homeless assistance grants, emergency shelter grants, and funds to municipalities to assist planning and infrastructure development are also provided. The federal funds require a small State match.

Energy Projects

\$20,750,000

\$250,000 Bond Funds

\$20,000,000 Fed Rcpts

\$500,000 I/A Rcpts

Reference No.: 38950

Category: Development

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005 - 06/30/2010

On-Going Project

Multiple federally funded energy programs of Bulk Fuel Upgrades, Rural Power Systems Upgrades, Alternate Energy and Energy Efficiency projects. This program contributes to the Department's mission of promoting a healthy economy and strong communities by providing economic growth in the communities it serves.

Ms. Hanrahan explained that this mostly federally funded program would fund a wide variety of energy programs including bulk fuel upgrades, rural power system upgrade programs, and alternative energy and energy efficiency projects.

Senator Bunde declared that he was "not looking forward to the day" when these federal funds might dissipate and the onus might be to replace them with general funds.

Language Section: Electrical Emergencies
\$330,000 Rural Elec
Reference No.: 32590
Category: Health/Human Services
Location: Statewide
Election District: Statewide
Estimated Project Dates: 07/01/2005 - 06/30-2010
On-Going Project

To provide technical support when an electric utility has lost the ability to generate or transmit power to its customers and the condition is a threat to life, health, and/or property in the rural community. This program contributes to the Department's mission of promoting a healthy economy and strong communities by providing economic growth in the communities it serves.

Ms. Hanrahan read the project description.

Language Section: NPR-A Impact Grant Program
\$29,517,700 NPR Fund
Reference No.: 38948
Category: Development
Location: Barrow
Election District: Arctic
Estimated Project Dates: 07/01/2005 - 06/30/2010
On-Going Project

Grants to communities for public facilities and services. Priority is given to those communities directly or severely impacted by the leases and development of oil and gas within the National Petroleum Reserve. This program contributes to the Development's mission of promoting a healthy economy and strong communities by providing economic growth in the communities it serves.

Ms. Hanrahan reviewed the project description.

Co-Chair Green asked that a list of the projects affected by this request be provided.

Ms. Hanrahan agreed to provide the information.

Co-Chair Wilken requested that this project be assigned to a subcommittee that he might chair, for further analyzing and development.

Co-Chair Green agreed.

Senator Stedman, Senator Dyson, and Senator Olson asked to serve on the subcommittee.

Co-Chair Green announced that Co-Chair Wilken would be the subcommittee chair.

Kodiak Launch Site Infrastructure

\$36,000,000 Fed Rcpts

Reference No.: 40008

Category: Development

Location: Kodiak

Election District: Kodiak

Estimated Project Dates: 07/01/2005 - 06/30/2010

One-Time Project

Kodiak launch site infrastructure to support the U.S. Department of Defense's Missile Defense Program. This program contributes to the Department's mission of promoting a healthy economy and strong communities by providing economic growth in the communities it serves.

Ms. Hanrahan stated this request would be federally funded. The intent is to bring the Kodiak launch site to meet federal Department of Defense requirements.

Protection and Education of Investors

\$300,000 Stat Desig

Reference No.: 40505

Category: Education

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005 - 06/30/2010

Protection and education of consumers/investors in accordance with a national securities settlement with 10 of the nation's top investment firms. This project contributes to the Department's mission of promoting a healthy economy and strong communities by educating the public in sound financial planning.

Ms. Hanrahan noted that this request is being withdrawn as it has been determined that rather than this money being directed to the

State, the State could recommend entities within the State that it could be directed to.

Senator Bunde suggested that the money be directed to the PERS and TRS retirement programs so that the systems could have an informed group of investors in regards to such things as the proposed Defined Contribution Retirement program.

Co-Chair Green thanked Senator Bunde for the suggestion.

[9:37:14 AM](#)

Morris Thompson Cultural and Visitors Center
\$250,000 Gen Fund
Reference No.: 40500
Category: Development
Location: Fairbanks Areawide
Election District: Fairbanks Areawide
Estimated Project Dates: 07/01/2005 - 06/30/2010
One-Time Project
Grant for the Morris Thompson Cultural and Visitors Center.

Ms. Hanrahan stated that this Center would provide visitor information services, visitor trip planning, environmental education, and exhibits. The total estimated cost of the Center would be \$26 million: \$15 million of federal funds and the remaining funds to be from the State and private contributors.

Co-Chair Green asked when the project might be completed.

Ms. Hanrahan replied that the conceptual design phase is reaching completion. Requests for bids have not been let. In order to complete the construction project by the spring of 2006, \$4.5 million must be raised in 2005. The final completion date is unknown.

Co-Chair Green asked whether this is the only budget request associated with the Morris Thompson Cultural Center.

Ms. Hanrahan replied that this is the only request being furthered by the Department. Further research regarding the project's total funding would be conducted.

Co-Chair Green commented that this item might be revisited.

[9:39:46 AM](#)

City of Valdez - Harborview Demolition

\$1,000,000 Gen Fund
Reference No.: 40517
Category: Development
Location: Valdez
Election District: Richardson/Glenn Highways
Estimated Project Dates: 07/01/2005 - 06/30/2010
One-Time Project
Demolition of Harborview building.

Ms. Hanrahan stated that the land on which this building sits was transferred to the City of Valdez. Since there is no viable economic use of the building, which was closed in 1997, the City is requesting funds to demolish and remediate the site. The building does contain hazardous materials.

Co-Chair Green asked whether the City of Valdez would be liable were any hazardous materials found.

Ms. Hanrahan asked for clarification whether the question pertained to liability during demolition.

Co-Chair Green expressed that the liability question pertained to both during and after demolition. In other words, would the State would have other obligation other than providing funds.

Ms. Hanrahan stated that further information would be provided.

Co-Chair Wilken asked the funding history attached to this project, as this is the seventh request to demolish this building that he has heard in as many years as a Member of this Committee.

Ms. Hanrahan stated that the information would be provided.

[9:41:53 AM](#)

Tongass Coast Aquarium, Inc.
\$100,000 Bond Funds
Reference No.: 40497
Category: Development
Location: Ketchikan Gateway Borough
Election District: Ketchikan
Estimated Project Dates: 07/01/2005 - 06/30/2010
One-Time Project

A grant for the Tongass Coast Aquarium, which will be a regional facility providing education, research and exhibits focusing on the coastal and marine ecosystems of Southeast Alaska. This project contributes to the Department's mission of promoting a healthy economy and strong communities by

providing educational opportunities and economic development in Southeast Alaska.

Ms. Hanrahan read the project description and stated that the funds would assist in constructing a 28,000 square foot aquarium.

Co-Chair Green asked that the funding history, to include the State's total obligation; the amount the federal government has provided; and other revenue sources, of this project be provided.

Ms. Hanrahan informed that this project is currently in the design phase. No formal bids have of yet been requested. The total cost is projected to be \$27 million. The total funding request to the State might range between one and four million dollars.

Co-Chair Green asked for clarification purposes, the amount being requested this year.

Ms. Hanrahan stated that the FY 06 request is for \$100,000.

Alaska Native Heritage Center

\$500,000 Gen Fund

Reference No.: 40498

Category: Development

Location: Anchorage Areawide

Election District: Anchorage Areawide

Estimated Project Dates: 07/01/2005 - 06/30/2010

One-Time Project

Grant to the Alaskan Native Heritage Center for the repair and construction of Alaskan Native village exhibit sites. This request contributes to the Department's mission of promoting a healthy economy and strong communities by assisting the tourism industry and those businesses benefiting from the tourism industry.

Ms. Hanrahan noted that this is the only Native educational and cultural center in the State that showcases the cultures of the State's native people "to the public and to school children". The Center is a premier tourist destination and, in partnership with an international and Alaskan tour operators, hosts approximately 100,000 visitors annually. It provides in excess of 100 jobs and is a marketing outlet for Rural handicrafts and cultural items.

Co-Chair Green asked whether this project could be supported by its revenues, private donations, and other resources.

Ms. Hanrahan expressed that this request would fund the construction of one village site and a playground within that site.

The overall plan is to construct five village sites that would represent the dwellings of each of the State's five regions.

Co-Chair Green pointed out that the request states that the funds would be for the repair and construction of exhibit sites. Ticket sales and other income processing venues should provide for the cost of repairs, as the project should be self-sustaining rather than continuing to request State funding.

Ms. Hanrahan stated that further information would be provided.

Lower Kuskokwim School District - The People's Learning Center
\$1,000,000 Gen Fund
Reference No.: 40502
Category: Development
Location: Bethel
Election District: Bethel
Estimated Project Dates: 07/01/2005 - 06/30/2010
One-Time Project
Grant to the Lower Kuskokwim School District for the construction of the Yuut Elitinaurviat, The People's Learning Center. This project contributes to the Department's mission of promoting a healthy economy and strong communities by providing educational opportunities in the community.

Ms. Hanrahan read the project description and noted that three million of the total eight million dollar project cost has been raised. Additional funding has been requested from the Alaska Native Education Grant Program, the Bureau of Indian Affairs, and from Alaska Congressman Ted Stevens' office.

[9:47:06 AM](#)

City of Unalaska - Boat Harbor
\$2,000,000 Bond Funds
Reference No.: 40501
Category: Development
Location: Unalaska
Election District: Bristol Bay/Aleutians
Estimated Project Dates: 07/01/2005 - 06/30/2010
One-Time Project
Grant to the City of Unalaska for a boat harbor at Little South America in Unalaska. This project contributes to the Department's mission of promoting a healthy economy and strong communities by providing infrastructure necessary for commercial enterprises and the community of Unalaska.

Ms. Hanrahan stated that this request would address "a serious lack

of moorage" in Unalaska. The breakwater construction would cost approximately \$11 million. While the City of Unalaska is responsible for the inner harbor improvements, this request would assist to support the total \$17 million project cost.

Senator Stedman asked whether additional funding requests, beyond this two million dollar request, might be forthcoming.

Co-Chair Green asked the Department to provide this information.

Senator Stedman also asked whether moorage fees and other income venues established by the City would sufficiently provide for on-going maintenance and replacement reserves for the project upon completion. The concern is that this harbor might be in a state of disrepair in 30 years as has been the experience with other harbors in the State.

Senator Bunde asked that information be provided about the plans to fund the on-going operating and maintenance costs of the Lower Kuskokwim School District - The People's Learning Center

Senator Olson asked whether the Unalaska boat harbor is located at the staging area site for the response to the December 2004 wreck of the tanker, the Selendang Ayu.

Ms. Hanrahan would clarify that information.

City of Cordova - Cordova Center

\$1,000,000 Gen Fund

Reference No.: 40503

Category: Development

Location: Cordova

Election District: Cordova/Southeast Islands

Estimated Project Dates: 07/01/2005 - 06/30/2010

One-Time Project

Grant to the City of Cordova for the construction of a Community Center in Cordova. This Request contributes to the Department's mission or promoting a healthy economy and strong communities by providing infrastructure necessary for commercial enterprises and the community of Cordova.

Ms. Hanrahan stated that this request would provide for a 32,000 square foot community center that would provide conference, convention, theater and training spaces; oil spill response training; an incident and emergency command and communication center; as well as space for a joint State and federal visitors facility. A public library for the elementary school might also be included.

Senator Bunde asked that information be provided regarding the funding source for the center's operations and maintenance needs.

Ms. Hanrahan stated that this concludes the Department's capital project requests.

Co-Chair Wilken understood that the Department might be requesting funds for a film project.

Ms. Hanrahan responded that no request in that regard is being presented.

AT EASE: [9:51:53 AM](#) / [10:04:59 AM](#)

Department of Corrections

Institution Closed Circuit TV System Recording
\$2,500,000 Bond Funds
Reference No.: 40267
Category: Public Protection
Location: Statewide
Election District: Statewide
Estimated Project Dates: 07/01/2005 - 06/30/2010
One-Time Project
Project will provide digital video recording systems within 11 Correctional Facilities statewide.

MARC ANTRIM, Commissioner, Department of Corrections, stated that this request would provide for closed circuit television and digital video recording systems through which to monitor prisoners. The first phase of the project would be the installation of cameras and the second phase would be the installation of the recording equipment. This project would expand the current system to allow the monitoring of living areas in addition to doorway and other traffic areas. In addition to reducing incidents of prisoner violence and property damage, the system would allow the Department to comply with federal laws enacted in 2003.

Deferred Maintenance, Repair, and Renovations
\$8,000,000 Bond Funds
Reference No.: 36788
Category: Public Protection
Location: Statewide
Election District: Statewide
Estimated Project Dates: 07/01/2005 - 60/30/2011
On-Going Project
Essential repair and renovation of electrical, mechanical,

roofing, fire/life safety, security, structural, food service, pavements and site drainage systems at all correctional facilities. This work is required to enable continued safe, secure and efficient operation of the 24-hour incarceration facilities.

Commissioner Antrim stated that this request would address the extensive list of deferred maintenance needs of the 117 facilities maintained by the Department. The majority of these facilities exceed twenty years of age; ten percent are at least 30 years old; and another ten percent exceed 40 years of age. A list of needs is included in the packet.

Statewide Equipment Replacement

\$450,000 Bond Funds

Reference No.: 30815

Category: Public Protection

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005 - 06/30/2011

On-Going Project

Replace essential security, life safety, food service, laundry, medical, records storage and maintenance equipment at all correctional institutions. This equipment is required to provide continued support of the officers and staff in confining incarcerated offenders and in maintaining safe operation of the institutions.

Commissioner Antrim stated that these funds would provide for the replacement of many critical items, including such things as snow removal equipment, grounds equipment such as lawnmowers, and fixed kitchen items such as stoves, steam kettles, and microwave ovens. Maintenance needs for such items has been deferred for many years.

Community Jails Life, Safety and Security Renovations and Miscellaneous Equipment

\$100,000 Bond Funds

Reference No.: 30818

Category: Public Protection

Location: Statewide

Election District: Statewide

Estimated Project Dates: 07/01/2005 - 06/30/2011

On-Going Project

This project funds essential safety and security renovations and equipment at fourteen (14) local governmental contract jails. These jails require repairs and modifications to continue their operation.

Commissioner Antrim noted that this request would provide necessary upgrades at 14 community jails that, while operated by the local community police departments, are under contract to the State. The upgrades would be akin to the upgrades that would be occurring at the State's jail facilities.

Co-Chair Green announced that this concludes the Department of Commerce, Community and Economic Development and the Department of Corrections capital project requests.

The bill was HELD in Committee.

#sb141

SENATE BILL NO. 141

"An Act repealing the termination date of certain provisions that require the reporting of social security numbers and automated data matching with financial institutions for child support enforcement purposes; relating to social security numbers on applications for commercial fishing licenses; and providing for an effective date."

This was the second hearing for this bill in the Senate Finance Committee.

Co-Chair Green noted that the sponsor's March 16, 2005 bill presentation has received positive reviews.

Senator Stedman, the bill's sponsor, informed the Committee that he would be addressing the information included in the "Retirement Security Act SB 141" handout dated March 17, 2005 [copy on file].

Co-Chair Wilken asked for further information regarding the graph titled "What went wrong?" that was included on page ten of the March 16, 2005 SB 141 handout [copy on file]; specifically the relevance to that graph of the language in the "Actuarial Value of Assets" paragraph that read, "Prior to 2002, Mercer used a 'corridor method'. Beginning in 2002 they switched to a 5-year 'smoothing method'".

Page 10

[March 16, 2005 SB 141 Handout]

What went wrong?

[Line graph showing Combined PERS & TRS Actuarial Valuations (2003): Accrued Liabilities, Actuarial Value Assets, and

Market Value Assets for the years 1994 through 2003. The data for 2003 is as follows.

Accrued Liabilities:	\$16,397,262
Actuarial Value Assets*	11,439,566
Market Value Assets:	10,994,074

*Asset Market Value is adjusted by the actuary in an effort to bring more order and predictability to the employer contribution rate and to smooth out year to year market fluctuations. Prior to 2002, Mercer used a "corridor method". Beginning in 2002 they switched to a 5-year "smoothing method".]

We Have Been Understating Our Liabilities For the Past Several Years

Senator Stedman responded that the page ten graph details the portfolio valuations beginning with the year 1994. The State's actuarial consultant, Mercer Actuarial Services (Mercer), utilized "a smoothing mechanism" during the first years reflected on the graph. This methodology amortized the portfolio's gains and losses over a five-year period, going forward. This assisted in smoothing out the employer contribution rate so that it would "not swing with the gyrations of the financial markets". However, as a result of the "extended" capital market upswing in the late 1990s, "the value of the portfolio [increased] up above targeted growth rates quite a bit," as reflected by the Market Value Assets line on the graph. Continuing utilization of the smoothing method would have produced "a substantially larger over-funding of the plan, assets to liabilities" and, the Actuary was concerned that the Boards might decrease "the employer contribution rate to unsustainable levels," with the possibility of reducing it to as low as zero. Therefore, Mercer changed the method for calculating the gains to the "corridor method", which established a "band" with a maximum 20-percent deviance from the market value. The band "artificially lowered the assets for the calculation of how far they were over-funded" as depicted by the line titled Actuarial Value Assets. The corridor method was utilized for several years during the "equity expansion or bull market" of the late 1990s.

Senator Stedman stated "that one of the items of correction" recommended by a 2001 audit was that the smoothing method with a five-year amortization schedule, be reinstated. This is the point in time reflected on the graph where the Accrued Liabilities line and the Market and Actuarial Value lines "substantially deviating away from each other".

Senator Stedman stated that in order to make that transition "it was necessary to bring the assets to market value". This endeavor

is depicted by the intersection of the Actuarial Value Assets and Market Value Assets lines on the graph in the year 2002.

Senator Stedman voiced that, moving forward to the year 2003, the Market Value Assets reflect a value of \$10,994,074 and the Actuarial Value Assets had a value of \$11,439,566. "The difference between those two numbers is just the five-percent smoothing or five-percent amortization of that loss going forward".

Senator Stedman communicated that this year the numbers would reflect "a gain" as the portfolio performed above the projected 8.25 percent target. That gain would be spread out over the next five years. The Legislature "as policy makers" should review both values, "recognizing that the Actuarial Value is just a value to sooth the contributions". Particular attention must be paid to Market Values, as that would reflect the portfolio's actual value.

[10:17:10 AM](#)

Page 14
[March 16, 2005 SB 141 Handout]

What went wrong?

[Bar graph showing Factors Contributing to PERS Employer Rate Increase* (% of Cumulative 1998 to 2003 Rate Increase Attributed to Each Factor) as follows:

Actuarial Loss (Increased Employer Rate)	
Assumption Changes	-34.19%
Investment Experience	-11.62%**
Health Experience	-11.28%
Demographic Experience	-8.89%
Asset Valuation Method	-4.42%**
Contri Shortfall Due to	
2 Year Calculated Rate	-3.37%
102% Funding Ratio	
Adjustments	-2.02%
Ad hoc PRPA	-1.56%
System Benefit Changes	-0.64%
Actuarial Gain (Decreased Employer Rate)	
Salary Experience	6.47%
Past Service Amortization	
Change	15.52%

*PERS Employer Rate increased 18.3% from 7.36% in 1998 to 25.63% in 2003

**Total Asset Side Impact of 16.04%

A Combination of Factors Created Our Present Situation

Senator Stedman informed that, as depicted on the page 14 chart in the March 16th handout, changing from the smoothing method to the corridor method and then back to the smoothing method placed "downward pressure on the Employer Contribution Rate"; amounting to 15.5 percent of a total 18.3 percent change in the Employer Contribution Rate between the years 1998 and 2003. "That was a positive. It lowered the contribution requirement down".

Co-Chair Wilken understood that had the smoothing methodology been the sole methodology utilized since 1994, the Actuarial Value Assets line might have tracked similarly to the Market Value Assets line on page ten's graph. He asked therefore whether the State would have the five billion dollar shortfall today, "had the decision been made to stay with the smoothing method and resisted the temptation to lower the Employer Contribution Rates because of the robust capital market".

Senator Stedman replied that the lines would have tracked "pretty close". However, had the Corridor Method not been implemented, the Public Employees Retirement System (PERS) and Teachers Retirement System (TRS) Boards "would have been under more pressure to lower" the Employer Contribution Rate, as it is doubtful that, at the time, the Boards "realized that their value of the assets were so under-valued; that liabilities they were looking at were not the actual liabilities", as he believed there was some miscalculation in the liabilities which "led to a false impression that they were at an artificially low level...if the liabilities would have been more accurately calculated back in the mid to late 90s it would have tracked almost on top of the market value of the portfolio and there would have certainly been no pressure to lower rates".

Co-Chair Wilken acknowledged the explanation. Continuing, he voiced that the State "depends a lot on our Actuary". To that point, he asked how much they are paid for their service.

Senator Stedman provided some "rough numbers"; approximately four million dollars has been paid to the Actuary between the years 1997 to 2005. The highest amount, \$717,000, was paid was in the year 2000. The targeted rate is \$500,000 a year. The forecast for 2005 is \$425,000. The "complex mathematical modeling work" that is conducted is extensive and it is "unfortunate that it was not as accurate" as he would have liked to have seen it in the late 1990s.

Senator Bunde, while acknowledging, "that this is a complicated field", voiced concern that were the answers not to one's liking, "we just change them to a different calculation until we get an answer that we like". He recalled, "being told by the experts ...

that the fund was basically over-capitalized. That we were contributing too much". Based on that advice, the Legislature made a decision within the past ten years to reduce its contribution, separate from the pressure applied to further reduce the contribution rate. He asked for confirmation that the Legislature's action was based on "information that we were over-capitalized".

Senator Stedman understood that some withdrawals had been made; however, this would have to be further reviewed.

Senator Bunde recalled the action occurring around 1994.

Senator Stedman acknowledged that something had occurred, but that his research has focused on recent years' activities. He affirmed that the action of removing assets from a plan when it is over-funded would "exaggerate" the problem were the day to come when the plan was under-funded.

Senator Bunde communicated that he was furthering this point because people are saying, "that the State screwed up, why should we have to increase our contribution". He declared that that the idea that "the Legislature reduced their contributions in an attempt to artificially show they were cutting the budget" is unfounded. The Legislative action taken was in response to advice from the PERS/TRS Boards who acted on the advice of the actuarials.

Senator Stedman clarified that in the late 1990s, both Boards lowered the employer contribution rate below what was recommended by the actuary. That action placed "more negative pressure on the system". Efforts to rectify this are being furthered in this bill.

Co-Chair Green understood that "some of that changing and lowering of rates was done without Legislative permission".

Senator Bunde believed this was the case with the latest change.

Senator Stedman calculated that a \$160 to \$190 million decrement had resulted from the lowering of the Employer Contribution Rates. While this is a lot of money, it is not, in the context of the overall five billion dollar shortfall.

Page 8

[March 16, 2005 SB 141 Handout]

What is the [status] of Alaska's system?

[Line graph showing Historical PERS & TRS Funding Ratios for each year from 1975 through 2003. The PERS ratio is 72.8

percent and the TRS ratio is 64.3 percent for 2003. Other information reads:

1975 System Population	
Active:	19,998
Retire:	1,734
2004 System Population	
Active:	43,300
Retire:	28,279
Terminated (Vested)	6,689
Terminated (Non-Vested)	14,606]

Senator Hoffman noted that the 70-percent PERS funding ratio for 2003, as depicted on the graph on page eight of the March 16, 2005 presentation, is approximately the same level as the 1980 funding ratio. Given the fact that economists and President George W. Bush proclaim that the economy is turning around and markets are rebounding, and, in light of the fact that page seven of the March 16th report indicates that 2006 would have a positive flow, he anticipated that the 2003 level would be the lowest point going forward. He asked whether the sponsor would agree. Continuing, he asked whether, in addition to the changes in the Employer Contribution Rates, there had been "any major changes" in the late 1970s or early 1980s that would have influenced the rebounding of the Funds or was it simply the growth of State government at the time. While he is not arguing against making management changes, he opined that the system has worked well.

Page 7

[March 16, 2005 SB 141 presentation]

What is the [status] of Alaska's system?

[Drawing of fuel barrel labeled with data specific to the Alaska system based on 2003 Actuarial Valuation. The barrel lists \$11.4 billion Net System Assets (Combined PERS & TRS Actuarial Asset Values) and \$16.4 billion Assets Needed to Meet Accrued Liabilities, with a difference of \$5.0 billion. Pipes attached to the barrel are labeled as follows.

Employer Contributions:	\$162.1 million
Member Contributions:	\$167.9 million
Investment Results:	\$373.1 million
Admin & Investment Expenses:	-\$32.6 million
Benefits & Refunds Paid:	-\$778.3 million

PERS & TRS Have A Combined \$5.0 Billion Unfunded Liability

Senator Hoffman observed that the graph on page seven of the March 16, 2005 presentation appears to be inverted, as the barrel's

contents should reflect the State's Net System Assets as two-thirds full rather than being depicted as one-third full. The graph, as presented "over-exaggerates" the situation.

Senator Stedman responded "it would be extremely difficult" to replicate the funding ratio trends of the late 1970s to early 1980s due "the magnitude" of today's experiences; specifically the number of employees, the number of retirees, and "escalating" health care costs issues. "From 1982 through 1990, a real strong capital market" assisted in increasing the values; and in the late 1970s and early 1980s, the State experienced a huge [economic] expansion.

[10:30:04 AM](#)

Senator Stedman shared that the Actuary would be providing their most recent funding ratio report soon, and it is expected that the funding ratios would decrease even though last year's portfolio performed above the projected 8.25 percent target. He reminded that the smoothing method calculations would amortize those gains over the next five years, and therefore, even though the funding ratios might reflect that the Systems are "in worse shape" ... "the real affect" is that "we are in a little bit better shape than we were a year ago". "From this point going forward" the situation is hopeful that another decline in the financial market would not be experienced for at least another two or three years. While the portfolio should move toward being fully funded, this would not occur "near as fast" as it did in the late 1970s and early 1980s.

Senator Stedman concurred that the barrel depicted on page seven could have been presented in the reverse. This would be corrected in the presentation going forward. The \$16.4 billion total liabilities and the \$11.4 billion in net assets were prominently displayed on page seven in order to clarify "what is full and what is empty". He agreed with Senator Hoffman that even though the State has a five billion dollar under-funding issue, "it is not anywhere near the point where we have a cash flow problem meeting our obligations" ... "There is no reason for any of the retirees or current participants to expect that their benefit levels are in jeopardy. That's not the issue".

Senator Stedman emphasized that one purposes of SB 141 is to restructure the PERS, TRS, and ASPIB Boards. One of the reconstituted Board's tasks would be to determine how to address the five billion dollar under-funding situation. "One of the solutions is just to ignore it; another one is to pay it off; and the other one is some combination" of the two. A multitude of options are available, but "the overriding factor that squeezes us on that under-funding" is employer contribution levels "relative to

the rest of their salaries ... "It squeezes the schools" and municipalities "to direct more money into current cash flow and to benefits". "It directs current cash flow today into benefits that were accumulated" in many cases over ten years ago. The issue of alleviating the pressure on cash flow must be addressed.

Senator Hoffman proclaimed that this bill would provide "major" alterations in the system, specifically the change in the Funds' management structure. He voiced concern regarding the "magnitude of the changes" being proposed considering that Alaska is in better shape than other states. Changes to the systems could be pursued after the initial focus of changing the management structure. Changing the whole process might jeopardize "the financial security and ability to draw employees back into State services". These things should be taken into consideration.

[10:35:28 AM](#)

Senator Bunde voiced that there is public perception that the Legislature "is trying to sneak this through too quickly". However, he attested that the discussion about changing from a Defined Benefit Plan (DBP) to a Defined Contribution Plan (DCP) has been occurring for at least ten years.

Senator Bunde noted that in 1975, there were approximately 2,000 active employees supporting approximately 1,700 retirees in the Retirement System; today, there are approximately 43,300 active employees and 28,000 retirees. "The ratio is diminishing". He asked whether the trend line might someday project one active employee per retiree.

Senator Stedman responded that the answer is yes. In 1975 there were 1,700 retirees, today there are 28,000 retirees, and there are another 20,000 individuals "who have some claim on the system were they come back in and work a few more years" and retire. This is one of the challenges in determining whether the trends of the late 1970s and early 1980s could be replicated. "There is a substantial waiting difference today concerning our retirees and the cash flow demands it places on the system." This is why, he agreed "with the conclusion drawn by the Actuary that you're not going to invest your way out of this situation at all".

[10:38:21 AM](#)

Senator Bunde responded that were everyone who had a claim on the Retirement System "to realize that claim, we would actually have one retiree for every worker making contributions to the System". That does not sound sustainable.

Senator Stedman affirmed that there are numerous Tier 1 former State workers who worked for the State in the 1970s and 1980s, who could be rehired and retire from the System with lifetime health benefits. This could amount to \$100 million in potential liabilities to the State. Were 20,000 former State workers to resume working for the State and then retire from the System, there would be more retirees than active employees. This scenario would occur anyway over the next 20 to 30 years as more people retire from the System. Even though the State's Retirement System is being challenged today, it is in a better situation than many other states that did not pre-fund their retirement systems. The State "should be congratulated" for having the foresight to pre-fund health care in its retirement system. This has assisted in addressing the situation Senator Bunde has alluded to where there is a one employee to one retiree ratio.

Senator Olson asked how the ratio might appear in ten years.

Senator Stedman responded that this information would be provided, as projections have been calculated for the next 25 years.

Senator Olson asked for further information regarding how the price of North Slope crude oil affected the funding status of the System as it relates to the trends of the PERS/TRS funding ratios depicted on page eight's chart.

Senator Stedman responded that the two largest impacts on the trend lines are the value placed on the Systems' liabilities and the value of the assets in the portfolio. The upward trend occurred during robust economic times even though there were "times of fluctuating oil prices". Aside from the impact that oil prices have on the economy, the retirement portfolio is not aligned with oil prices.

Senator Olson applauded Senator Stedman's efforts to address the \$5.5 billion liability, and stated that any delay would only exacerbate the problem.

Co-Chair Green added that "the natural inclination is for people to turn to the State for assistance to backfill and to make good on" future increases. There is a point at which the State "might lose all incentive" to continue to fund that shortfall. This would result in a drop-off in employment, as entities could not continue to employ people when the employer contribution rate increases upwards of 50-percent of the salary just to pay for benefits. This is why developing a solution to the issue has become "very important".

Senator Stedman turned the Committee's attention to the handout dated March 17, 2005. He noted that with any major piece of legislation, substantial modifications would be expected.

Page 3
March 17, 2005 handout

SB 141 Walk-through

Our analysis looked at both components of the problem
With the goal of developing solutions

Structural Component

To identify the systemic Problems in PERS/TRS

1. How do we prevent this from happening again?
2. How can we fix the system and bring it back Into balance?
3. How can we better predict and control costs going forward?

Financial Component

To identify the causes of our liability growth

1. How can we stabilize future Employer contribution rates?
2. How can we provide near term financial relief to employers?
3. How do we develop a long solution to funding the \$5.0 Billion gap?

Senator Stedman stated that the decision was made not to develop a financial component to fix the five billion dollar shortfall in this legislation. It was determined to be more important to deal with the structural component in terms "of how we got here and then after that deal with the under-funding issue because you have to stem the hemorrhage". Efforts to address how to prevent this situation from re-occurring would include working with the State's actuaries and the boards to justify the values of the assets and the liabilities to ensure that the most accurate numbers are being presented. Efforts to address fixing the system would involve a Board restructuring in that one entity would be involved in addressing both the assets and liabilities so that no "buck passing" would occur. Efforts to predict and control costs going forward would be addressed as the bill progresses.

Senator Stedman stated that the financial side of the equation must address stabilizing the employer contribution rates, and if possible "lower them because of the squeeze-out affect it has on today's cash flow to pay yesterday's benefits for the employees has a lot of negative impacts all across the State". The issue of providing near term financial relief to employers would be addressed after this legislation is implemented, as the new Board would address the shortfall issue and present recommendations

regarding how to address them. That would be an entirely separate process.

[10:46:22 AM](#)

Senator Stedman stressed that the five billion dollar shortfall is an obligation under the Employers Defined Benefit Plan. "It is not the employees' problem per se, they did not create this issue". The Normal Cost factor is the funding that an employee contributes today for benefits accumulated for the future. There is an abundance of accumulated Past Service benefits that must be paid for today. This is an area that the new Board would be addressing. The question is what would be a "reasonable" employer/employee contribution split under today's economic conditions with rising health care trends. Currently PERS employers pay 66-percent and the employees pay 34-percent. The bill includes a provision that the contribution levels be reviewed in order to determine whether modifications to the splits would be necessary. This issue should not be ignored.

page 4
March 17, 2005 handout

We considered the Administration's 2004 Tier Committee work during our analysis and in our solutions
Tier Committee Data Reviewed:

- Tier Alternative Recommendations
- Employer survey
- Member focus group results
- Benchmarking
- Benefit levels
- Demographic projections
- Implications of Medicare changes
- Trends, issues and alternative
- Cost analysis and projections

[10:49:04 AM](#)

Senator Stedman reminded that a year earlier, the Senate Finance Committee had requested the PERS/TRS Boards to review Tier structures and alternatives. The Boards' Tier Review subcommittee had conducted a vast amount of work as depicted on page four. The Boards had not, however, adopted either of the two tier alternatives that had been recommended: one being a combination of DBP and DCP and the other a pure DCP.

Senator Stedman stated that upon review of the Tier Review subcommittee's report, the pure DCP plan was furthered in this legislation.

Senator Bunde shared that "a surprising number of people" have communicated that it increasingly difficult to hire talented people to work for the State. The concern is that were benefits changed, it would further acerbate this situation.

Senator Stedman responded that this concern was reviewed with the determination being that this might or might not be a factor, determining on how the benefit package was structured. A tier structure detrimental to retention and hiring should not be developed. The contribution level issue would be addressed by the Committee. "A blanket statement that a defined contribution plan is at a disadvantage to defined benefits is just not true. It depends on the structure of both plans". A tier must be developed that would be comparable to Tier III. Were both salary and benefits levels reduced to the point where the State was "disadvantaged in the market place" then "the organization would be hurt". It is necessary that the employer be provided built-in flexibility so that in the event that were to occur, they could respond.

Senator Olson asked regarding the stabilizing employer contribution rate component identified on page three; specifically what assurances would be made to protect the employee. It would be unacceptable to place this burden on the employee when it was the result of poor investment strategy on the part of the Boards.

Senator Stedman replied that in his opinion "it is not the obligation of the employee to fund that five billion dollar shortfall, it is an obligation of the employer". "This is part of the risk inherent in a Defined Benefit Plan". Were inadequate contributions made and were there to be an inadequate investment performance, it remains the employers' responsibility to meet the obligations. "This is an important point: the employee", either current or retired, is not at risk of loosing their benefits. Were any employee contribution adjustment to be made, it would not be utilized to address the five billion dollar under-funded liability from the past. These are two separate issues: the benefits being accumulated today for today's service as compared to the benefits that were accumulated in the past.

[10:54:44 AM](#)

page 5
March 17, 2005 handout

SB 141 Walk-through

Defined Benefit Plan

- *Benefit level is fixed
- *Benefit is based on a
- *Formula involving salary, years of service, age, etc
- *Benefit is paid for life and to qualified survivors
- *Future benefit payments are NOT affected by the plans funding level

Defined Contribution Plan

- *Contribution level is fixed
- *Benefit is based on the amount of money invested and earned in employee's account
- *Benefit is paid until account runs out
- *Future benefit payments are driven by investment performance

Senator Stedman explained that this page compares a DBP to a DCP. A DCP would resemble a 401(K) plan whose contributions would be invested in pre-determined investment portfolio options from which an employee could choose.

page 6
March 17, 2005 handout

SB 141 Walk-through
Defined Benefit Plan

- Advantages:
- *Pooling of longevity risk
 - *Guaranteed income stream
 - *System favors longer-service employees

- Challenges:
- *Employer bears investment risk
 - *Estimation of Liabilities
 - *Rising health costs
 - *Unpredictable or uncontrollable costs

Defined Contribution Plan

- Advantages:
- *Portability
 - *Self-directed investing
 - *Contribution equity among employees
 - *Predictability
 - *Stable costs
 - *Shifting of investment risk
 - *No long-term administrative costs

- Challenges:
- *Workforce management
 - *Employee education
 - *Accurate retirement planning

Senator Stedman reviewed the advantages and disadvantages of each plan.

[10:59:58 AM](#)

Senator Hoffman stated that since one of DBP's listed challenges is that the employer bears the investment risk, it should be listed under the DCP's challenges that the employee bears that investment risk.

Senator Stedman agreed and noted that this was the intent of the "Shifting of investment risk" under the Advantages component of the DCP. The information would be changed to better reflect that risk shift.

page 7
March 17, 2005 handout

SB 141 Walk-through

	Current PERS Tier I/II & TRS Tier 1 DB Plan	Current PERS Tier [III] & TRS Tier II DB Plan	Senate Bill 141 DC Plan .
PERS Employee Contribution Rate	6.75% other 7.5% Police/ Fire 9.6% school district	6.75% or 7.5% Police/Fire 7.5% Police/Fire 9.6% school district	8% all members voluntary % up to IRA limits
TRS Employee Contribution Rate	8.65	8.65%	8% all members
Vesting	5 years PERS 8 year TRS	5 years PERS 8 year TRS	Immediate for employee contributions Fully vested in employer contributions after 5 years
Retirement Age	55 normal- 50 early 30 years "all others" 20 Police/Fire 20 Teachers	60 normal- 55 early 30 years "all others" 20 Police/Fire 20 Teachers	Any age
PERS and TRS Benefit	2% up to 2.5% multiplier	2% up to 2.5% multiplier	11.5% per year to DC

Formula	per year DB Multiplier x years of service x high 3 years avg salary	per year DB Multiplier x years of service x high 3 (TRS) years or 5 (PERS) years avg salary	account + investment earnings. HRA account accumulated over working lifetime
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Senator Stedman pointed out that the third column's heading should correctly identify Tier III rather than Tier II/III. He noted that page eight provides the breakout details for the medical and normal costs components for these components.

Senator Stedman referred the Committee to a separate five-page March 17, 2005 handout titled "SB 141 Walkthrough" [copy on file]. That material includes Section numbers and pages numbers which correspond to language in the bill. The "heart" of the proposed benefit tier is the Defined Contribution Plan.

SB 141 Walkthrough

Defined Contribution (DC) Plan Elements

*Required Contributions

- Employee: 8.0% of compensation, deducted pre-tax by employer. Sec.14.25.340(pg 13), Sec.39.35.730(pg 64).
- Employer: 3.5% of employee compensation. Sec.14.25.350(pg 14), Sec.39.35.740(pg 70)
- Total individual account contributions: 11.5%

*Optional Contributions

- A member may elect to contribute additional earning not to exceed the limits established by the Internal Revenue Code. Sec. 14.25.340(b)(pg 13), Sec. 39.35.730(c) (pg 69)

Senator Stedman reviewed the components of the retirement benefits. The medical benefits component would be addressed separately. Outlining the various components in this manner would allow for them to be addressed during discussions with the Board.

*Vesting Sec. 14.25.390(pg 16), Sec. 39.35.790(pg 72)

- All members of the DC plan are immediately vested in their own contribution and related earnings.
- Members are gradually vested in the employer contributions and related earning on the following schedule.

= 25% after two years

- = 50% after three years
- = 75% after four years
- = 100% after five years

*Rollovers Sec. 14.35.360(pg 14), Sec. 39.35.760(pg 70)

- Employees can take their individual account with them when they leave employment.
- Employees can "roll" in other qualified funds when they are hired.

Senator Stedman noted that were the employee to terminate service at any time, their employee contributions would accompany them at full value. Were the employee to leave State employment after five years, they would be entitled to 100 percent of employer contributions. These employer contributions would be portable in that the employee could roll them into their individual IRA or to subsequent employers' 401(k) plans. The portability component is beneficial as the national employment trend is that people would "have multiple careers during their working lifetime". The national trend is toward making retirement plans portable from one job to another.

[11:05:10 AM](#)

Investments of Accounts Sec. 14.25.400(pg 16), Sec. 39.35.800(pg 72)

- The Alaska Retirement Management Board will provide a range of investment options.
- Participants direct the investment of their funds.

Distribution of Accounts

- Employee may elect a distribution of funds upon termination of employment, after 60 days. Sec. 14.25.410(pg 17) - Sec. 14.25.430(pg 19), Sec. 39.35.810(pg 73)-Sec. 39.35.810(b) (pg 73)
- Subject to IRC regulations.
- May receive funds prior to 60 days for financial hardship. Sec. 14.25.410(b) (pg 17), Sec. 39.35.810(b) (pg 73)

Senator Stedman stated that the investment options would be similar to those offered in the Supplemental Benefits System (SBS). The employees "would bear the risks and the rewards". The employee could remove their funds from the system 60 days after terminating employment.

[11:06:04 AM](#)

Senator Bunde asked regarding the frequency of the retirement disbursement.

Senator Stedman stated that this would be developed as the language progresses. However, the list of available options would include the mandatory age 70.5 distribution. "Most people would take this plan and roll it into their IRAs upon separation of service" or the employer would have "a whole range" of options through which to address monies left in the System.

Senator Bunde shared a constituent's question regarding whether there was a safety net through which to address the needs of someone who upon retirement, might have invested poorly or expended all their funds.

Senator Stedman responded that the investment options provided by the Alaska Retirement Board would have standard selections. However, were someone to retire, the employer would not be held responsible at that point forward. The employer would provide a multitude of investment information.

[11:09:23 AM](#)

Medical Program Elements

- Required Contribution by Employer Sec. 14.25.480(pg 24), Sec. 39.35.870 (pg 80)
- 3.75% of employee compensation.
- Contribution is made to group health and life insurance trust fund to be used for employer share of retiree's monthly medical premiums.

TRACI CARPENTER, Staff to Co-Chair Green, reviewed the medical components of the bill, which she attested define "where the concept of retirement really comes" into play in the DCP. The contribution rate of the employer would be set at 3.75 percent, as recommended by Mercer. This rate "is considerably lower than the current nine percent".

Retirement Sec. 14.25.470 (pg 24), Sec. 39.35.870 (pg 80)

- Retirement from the DC plan is required to obtain access to major medical insurance and the health reimbursement arrangement (HRA)
- Access means that an eligible person may not be denied insurance coverage except for failure to pay the required premium.

- A member is eligible to retire if they have reached:
 - = normal retirement age of 65 and has minimum of 10 years; or
 - = has 25 years of service for peace officer/firefighter; or
 - = has 30 years of service for all others; and
 - = has been an active member for at least a year prior to retirement.

[11:13:43 AM](#)

Ms. Carpenter read the retirement components and stated that a person must be: employed for a minimum of one year before they could apply for retirement and must meet the age and service requirements.

Major Medical Insurance Sec. 14.25.480 (pg 24), Sec. 39.354.880(pg 80)

- A member who meets the retirement provisions is eligible to enroll in the retiree major medical insurance plan.
 - = Insurance coverage includes the spouse and dependent children of the retiree.
- The surviving spouse of a retiree who was enrolled in the retiree major medical insurance plan is also eligible to enroll.
 - = Insurance coverage includes the dependent children of the surviving spouse.
- Retirees who meet the required years of service, but who are less than Medicare age eligible (presently 65), must pay the full premium to receive coverage.
- Retirees who are Medicare age eligible will pay only the portion of monthly medical premiums depending on years of service:
 - + 10-14 years = 30%
 - + 15-19 years = 25%
 - + 20-24 years = 20%
 - + 25-29 years = 15%
 - + 30+ years = 10%
- Only one premium per retiree and family.
- Different premiums developed for single retirees and retirees with spouse and/or children.

Ms. Carpenter reviewed the Major Medical Insurance component.

Health Reimbursement Arrangement (HRA) Sec. 39.30.300(pg 47)
Required Contributions

= Employer contributes an annual amount per employee to the

health insurance trust fund.

- = Calculation is 1% of average annual employer group compensation, to a maximum of \$500.
- = Contribution is recorded in both an individual employee record of account and an employer record.
- = Interest is posted to individual records annually, the rate determined by the ARMB.
- = Contributions and interest accumulate over working lifetime of employees.

Employer Fund Sec. 39.30.350(pg 48)

- = The HRA Trust is an employer owned fund.
- = Individual accounts of record are maintained for five years if an employee terminates without retiring.
- = Terminated employee accounts revert to the employer unless the individual returns to work within the five-year period.
- = A person who returns to work within the five-year period is attributed the account balance recorded in their name on the date of termination.
- = Employers may use surplus funds held in the trust to credit individual employee records with the annual contributions owed by the employer.

Reimbursements

= Who is eligible? Sec. 39.30.390(pg 48)

+ Members who retire directly from the system plus their spouse and dependent children

+ Spouse and dependent children are still eligible if the retiree dies

+ Dependent children are still eligible if both retiree and spouse die.

= Reimbursements made for qualified medical expenses under (RC 213(d), including medical premium payments. Sec. 39.30.400 (pg 49)

= Total reimbursements are limited to an individual's recorded amount.

= No set limits other than exhaustion of account balance.

Ms. Carpenter stated that the "HRA is a new feature". The idea is to have a separate fund to which the employer contributes a specified dollar amount for each employee. The employer group compensation method would "ensure equity" for each employer as the amount is based on a groups' average salary. The fund would be an employer owned fund in that employees do not contribute to it. Funds that revert to the Trust could be utilized by the employer to prepay future contributions.

[Note: Senator Bunde assumed chair of the meeting.]

Senator Bunde asked Senator Stedman to, when appropriate identify the component of the bill that would provide flexibility to address such things as recruiting challenges.

Senator Hoffman referenced earlier comment that one of the good elements of the State's current medical program is that it is prepaid. To that point, he asked how this plan would compare.

Senator Stedman opined that an employee would prefer to have a defined benefit plan for health care in that after a specified number of years, medical benefits "are provided for life with no risk sharing of the premium cost increases into the future". However, from an employer's standpoint, this would not be preferred due to the risk level associated with it and the difficulty the employer has in calculating future years' levels of liability. The DCP being proposed would provide that an employee who separates from the State early would be required to pay some portion of their own health insurance premiums until they reach the age of 65.

[11:20:15 AM](#)

Senator Stedman stated, therefore, that the answer to the question would depend on whether the employer or the employee is answering it. There is a trend to move away from DBP "due to the inherent risk level for the employer".

[Note: Co-Chair Green resumed chair.]

[11:21:32 AM](#)

Senator Stedman responded to Senator Bunde's question regarding the flexibility that could be provided to address recruitment difficulties by stating that one of the disadvantages recognized by employers in the current system is that the fact that it is embedded in the State's Constitution does not provide a lot of flexibility were adverse conditions to arise. Under the new tier proposal there would be flexibility in that the employer contribution rate levels could be discussed. Some adjustments could be made to the rates being proposed. Were the State to face recruitment or retention challenges in the future, the ability to revisit the rate would be provided. "It is very difficult to take something away, but it is very easy to increase it".

Senator Bunde understood therefore that "the current systems that are inscribed in Constitution are inflexible by definition". This new system would not be embedded in the Constitution and would therefore have some flexibility.

Changes to Existing Retirement System

Consolidation of Boards

- Eliminates:
 - = Public Employees' Retirement System Board
 - = Teachers' Retirement System Board.
 - = Alaska State Pension Investment Board.
- Creates new Alaska Retirement Management Board (ARM Board) Sec. 37.10.210 (pg 36)
 - = 9 trustees appointed by the Governor
 - + Commissioner of Administration
 - + Commissioner of Revenue
 - + 3 Alaska residents who do not participate in the retirement system
 - + 1 finance officer of a political subdivision
 - + 1 finance officer of a school district
 - + 1 PERS member (active or retired)
 - + 1 TRS member (active or retired)
 - = All trustees must have recognized competence in one or more fields of investment management, finance, banking, economics, accounting, pension administration, or actuarial analysis
 - = Terms
 - + Staggered three years
 - + Limited to three consecutive terms with a required one-year break

Senator Stedman emphasized that the three current boards, the PERS, TRS, and ASPIB Boards, would be consolidated into one Board, the Alaska Retirement Management (ARM) Board, that would consist of nine members.

[11:25:21 AM](#)

Authority and Responsibility of ARM Board Sec. 37.10.220 (pg 38), Sec. 39.30.155 (pg 46)

- Manage the assets of the defined benefits trust fund to meet pension liabilities.
- Annual actuarial valuation of system plans, coordinating with the retirement system administrator.
- Analysis of actuarial assumptions experience:
 - = Health costs assumptions annually.
 - = All other assumptions not less than every four years.
- Audit of actuary not less than every four years.

- Rate setting:
 - = Employer contribution rates, including "normal cost" and "past service cost".
 - = Employer contribution rates to the extent that the normal cost rate increases so that 50 percent would be higher than the current rates set in statute.
 - = Interest rates credited to individual employee accounts.
 - = Interest rates credited to employee HRA account records.
- Provide a range of investment options for all employee-directed accounts.

Senator Stedman stated that the goal is to manage the assets of the DBP Trust to meet pension liabilities. Both should be considered when decisions are being made. Mismatching these components has resulted in today's situation. The specified actuarial and assumption reviews would assist in keeping the system "on track". The rate setting components for Normal Cost and Past service Costs, which are two separate items, must be considered in rate setting. This bill would propose, for a discussion starting point, the Normal Service Cost being split approximately 50/50 between the employer and the employee. Currently that split is approximately 66 percent employer and 34 percent employee. This would increase the employee contribution. After discussion, the decision might be to not increase the employee percentage.

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Other Duties of the former PERS and TRS Boards Transferred
Sec. 39.35.005(pg 53)

- To the Commissioner of Administration:
 - = Adoption of regulations governing the retirement systems
 - = Requests for a waiver of any adjustment made to the retirement system accounts due to a change or error in contributions or benefit computations.
- To the Office of Administrative Hearings: Sec. 109(pg 90)
 - =Adjudication of appeals related to decisions of the retirement system administrator.
 - =Adjudication of appeals related to the denial of a waiver for repayment of overpayments.

Senator Stedman stated that due to the fact that this legislation would eliminate the PERS and TRS Boards, other duties of the Boards must be re-directed.

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Senator Stedman noted that as organized labor groups weight in on the proposals, adjustments to such things as the contribution rates might need addressing. He reiterated that a "clear distinction must be made" between the Normal Service Cost and the Past Service Costs.

Senator Stedman stated that the Committee has been provided a handout titled "Alaska Retirement System Boards" [copy on file] dated March 17th, 2005 that provides comparisons between the current systems and the proposed system.

Senator Stedman stated that this concludes his remarks for the day. The hope is to provide the information to the public "in order to facilitate a robust discussion of the pros and cons" of the proposal. Amendments could be presented to further the development of "a new tier proposal that is fair and comprehensive not only to the employees, but to the State and to the citizens of the State".

Senator Hoffman asked whether the Past Service Cost obligation, which "would be calculated at the time of transition" at approximately \$5.5 billion, would have an interest rate attached to it and whether a timeframe had been established in which to address that obligation.

Senator Stedman responded that the Past Service Cost's \$5.5 billion unfunded liability "would not change with the creation of a new tier" and would remain with the structure associated with Tiers I, II and III. Existing employees would continue under the terms of the existing tiers with the exception being that new employees would be provided the option of transferring to the new tier if they so desired. New employees would be subject to the new tier.

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Senator Hoffman commented that, at some point, the employer must address the Past Service Cost obligation. Therefore, he asked how that obligation would be addressed.

Senator Stedman, expressing that Senator Hoffman is making a "good point", stated that the proposed 50/50 employer/employee contribution spilt would only apply to the Normal Service Cost. "The Past Service Cost is a separate entity not related to any 50/50 split". He understood that there would be no legal obligation on the part of current and retired employees "to go back and help the State with the Past Service Cost. That is a liability of the

State". The 50/50 split pertaining to the Normal Service Cost is included "to recognize that there has been large changes in the cost of health care and benefits over the last couple of decades". It was considered "prudent" for the State to include this ratio split as a point of discussion. The question is whether the current 66/34 employer/employee contribution "split is fair" or should it be changed to the proposed 50/50 split or some point in between. The five billion dollar under-funding liability does relate to the Past Service Cost.

Senator Hoffman acknowledged that the liability does relate to the Past Service Cost, but stated that "at some point" that liability must be paid off. In that regard, he asked whether a plan has been developed under the current three tiers whereby that obligation would be paid off or whether "that's the life of the retirement and once those people retire then its magically paid off at that point".

Senator Stedman responded that the Committee could issue a decision that the debt would never be paid off; that some portion of it would be paid; or that it could be dealt with in ten, 15 or 20 years. This discussion should be addressed after the new Board is established and had an opportunity to review the situation and make recommendations.

Senator Hoffman understood therefore that the employer contribution rate components included in this legislation are applicable to the Normal Cost Rate. The Board would address the Past Service Cost rates. The State would continue to be obligated to fund the Past Service Cost liability. "That bill is going to come due someday".

Senator Stedman replied that the Past Service Cost debt was not addressed in this bill "due to the complexity of the issue". "A clear distinction" between the Normal Cost Rate issues and the Past Service Cost rate issues must be defined as, it would be easy for people to incorrectly assume that an employee payment structure would be implemented in order to address the debt.

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Senator Stedman opined that separating these issues would allow for an orderly analysis of the five billion dollar debt to be conducted.

Senator Hoffman stated that the five billion dollar debt is the reason "we are here". Making "this monumental change without addressing the reason why "we are here is not fulfilling our obligation".

Senator Stedman expressed that the five billion dollar debt is the result of systemic problems in the system. The systemic problems must be identified and fixed before the resulting five billion dollar debt issue could be addressed. Were money allocated to address the debt without fixing whatever created the debt, the situation might "reoccur in the future".

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Senator Stedman stressed that this "is why this is a two-step process". It is hopeful that this legislation would be adopted and then the five billion dollar debt could be addressed.

Ms. Carpenter noted that this legislation would not change the manner in which the employer contribution rates are calculated. Currently the Actuary calculates the unfunded liability, which is the Past Service Rate. It is amortized over 25 years with an approximate four-percent interest rate, which the employer is required to pay. The FY 06 Employer Contribution rates are projected to be 25.62 percent for PERS and 38.85 percent for TRS. These escalating employer contribution rate levels for benefits are "the big problem" that employers are facing each year.

Co-Chair Green asked whether a continual increase in the rates is projected.

Ms. Carpenter responded that, for the next 25 years, the PERS rate is projected to increase to the 30-percent range and TRS rate is projected to increase to approximately 50-percent.

Co-Chair Green concluded therefore, that not doing anything would contribute to the continuance of the problem. Changing the system would at least stop the trend established by the current system. Something must change in the system to address the problem.

Senator Olson found it "inconceivable that the idea of not paying for the liability would even be on the radar screen".

Senator Stedman responded that, in his opinion, "it is not a viable option". A variety of options could be presented, to include paying the debt if the State had the money or "to ignore it and let the plan run". Neither of those options is acceptable. The answer might be somewhere in the middle. Some plan must be developed through which to alleviate the burden placed on the employers. Otherwise, its continuance would be detrimental to the economy of the State. "It shifts too much cash flow into employee benefits that were accumulated"

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Senator Stedman concluded that the solution would be somewhere in the middle. Ignoring the problem "is not the solution and we don't have the ability to write a check and fund it". Even were money available, the root of the problem must be addressed. Mechanisms could then be developed through which to address the debt.

Senator Olson declared that efforts must be taken "to insure that the employee does not come out on the short side".

The bill was HELD in Committee.
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ADJOURNMENT

Co-Chair Green adjourned the meeting at 11:45 AM.