ALASKA STATE LEGISLATURE
HOUSE STATE AFFAIRS STANDING COMMITTEE
March 31, 2007
10:07 a.m.

MEMBERS PRESENT

Representative Bob Lynn, Chair
Representative Bob Roses, Vice Chair
Representative John Coghill
Representative Kyle Johansen
Representative Andrea Doll
Representative Max Gruenberg

MEMBERS ABSENT

Representative Craig Johnson

COMMITTEE CALENDAR

HOUSE BILL NO. 179
"An Act relating to insurance for public employees, teachers, and certain retired public employees and teachers and to supplemental employee benefits; relating to teachers' and public employees' defined benefit retirement plans, to teachers' and public employees' defined contribution retirement plans, to employee and employer contributions to the teachers' retirement system and the public employees' retirement system, and to the administration of the Public Employees' Retirement System of Alaska and the deferred compensation program for state employees; establishing in the Department of Revenue the teachers' retirement system past service cost liability account and the public employees' retirement system past service cost liability account; relating to benefits of, references to federal law in, and investments in the teachers' retirement system and the public employees' retirement system; modifying the jurisdiction of the independent office of administrative hearings as related to retirement and related personnel benefits; and providing for an effective date."

- HEARD AND HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 179
SHORT TITLE: PUBLIC EMPLOYEE/TEACHER RETIREM'T SYSTEMS
SPONSOR(s): REPRESENTATIVE(s) KELLY

03/05/07	(H)	READ THE FIRST TIME - REFERRALS
03/05/07	(H)	STA, FIN
03/29/07	(H)	STA AT 8:00 AM CAPITOL 106
03/29/07	(H)	Heard & Held
03/29/07	(H)	MINUTE(STA)
03/31/07	(H)	STA AT 10:00 AM CAPITOL 106

WITNESS REGISTER

REPRESENTATIVE MIKE KELLY
Alaska State Legislature
Juneau, Alaska
POSITION STATEMENT: As prime sponsor of HB 179, reviewed the bill's main objectives.

LARRY SEMMENS
Kenai, Alaska
POSITION STATEMENT: Testified during the hearing on HB 179.

LYDIA GARCIA
Interim Executive Director
National Education Association of Alaska (NEA-Alaska)
Anchorage, Alaska
POSITION STATEMENT: Testified on behalf of the 13,000 members of NEA-Alaska in opposition to HB 179.

ROD L. BETIT, President/CEO
Alaska State Hospital and Nursing Home Association (ASHNHA)
Juneau, Alaska
POSITION STATEMENT: Testified in support of the 80/20 split proposed in HB 179.

GAVIN D. CHARRIER
Local 6137 Alaska Public Employees Association/American Federation of Teachers (APEA/AFT)
Ketchikan, Alaska
POSITION STATEMENT: Testified on behalf of himself and the Local 6137 APEA/AFT during the hearing on HB 179.

JIM DUNCAN, Business Manager
Alaska State Employees Association Local 52
Anchorage, Alaska
POSITION STATEMENT: Testified on behalf of the approximately 8,200 general government unit employees in Alaska in opposition to the provisions of HB 179 related to the increase in employee contribution of 5 percent.

MICHAEL E. LAMB, CPA, CGFM, Chief Financial Officer
Fairbanks North Star Borough
Fairbanks, Alaska
POSITION STATEMENT: Offered suggestions during the hearing on HB 179.

DUANE MORAN, President
Anchorage Council of Education
Anchorage, Alaska
POSITION STATEMENT: Testified that he takes significant issue with the portion of HB 179 which proposes a [5 percent] increase in employee contributions.

RICK SCHIKORA
(No address provided)
POSITION STATEMENT: Testified on behalf of himself during the hearing on HB 179, in support of Representative Kelly's efforts to "get everybody to come to the table."

GARY HUTCHINSON
(No address provided)
POSITION STATEMENT: Testified on behalf of himself during the hearing on HB 179.

JASON AVERY
Fairbanks, Alaska
POSITION STATEMENT: Testified on behalf of himself in opposition to the 5 percent increase in employee contributions proposed in HB 179.

DAN WAYNE, Attorney
Legislative Legal and Research Services
Juneau, Alaska
POSITION STATEMENT: Answered questions during the hearing on HB 179.

ACTION NARRATIVE

CHAIR BOB LYNN called the House State Affairs Standing Committee meeting to order at 10:07:44 AM. Representatives Roses, Coghill, Johansen, Gruenberg, Doll, and Lynn were present at the call to order.

HB 179-PUBLIC EMPLOYEE/TEACHER RETIREM'T SYSTEMS

[Contains mention of HB 191.]

CHAIR LYNN announced that the only order of business was HOUSE BILL NO. 179, "An Act relating to insurance for public employees, teachers, and certain retired public employees and teachers and to supplemental employee benefits; relating to teachers' and public employees' defined benefit retirement plans, to teachers' and public employees' defined contribution retirement plans, to employee and employer contributions to the teachers' retirement system and the public employees' retirement system, and to the administration of the Public Employees' Retirement System of Alaska and the deferred compensation program for state employees; establishing in the Department of Revenue the teachers' retirement system past service cost liability account and the public employees' retirement system past service cost liability account; relating to benefits of, references to federal law in, and investments in the teachers' retirement system and the public employees' retirement system; modifying the jurisdiction of the independent office of administrative hearings as related to retirement and related personnel benefits; and providing for an effective date."

10:09:06 AM

REPRESENTATIVE MIKE KELLY, Alaska State Legislature, as prime sponsor of HB 179, reviewed that the bill's main purpose is to address the $10 billion unfunded liability of the Public Employees' Retirement System (PERS) and Teachers' Retirement System (TRS). He noted that PERS is currently funded at 65 percent, while TRS is currently funded at 60 percent. The bill proposes that the state pick up 80 percent of the unfunded liability obligation, while the employers pay 20 percent of the obligation. Those in the plan would contribute 5 percent toward current period costs.

10:12:52 AM

CHAIR LYNN asked Representative Kelly to confirm that the 5 percent would not be used as "a penalty to the new employees to pay for the sins of whatever caused the unfunded liability in the past."

REPRESENTATIVE KELLY confirmed that is true.

10:13:36 AM

REPRESENTATIVE ROSES asked where the monies from the 80-20 split would go.

REPRESENTATIVE KELLY replied that those monies are reserved with a present value for future payments over the lifetime of the employee.

REPRESENTATIVE ROSES stated his understanding that currently there are two pools of money: one is generated as a result of those called, "active employees." A contribution is made by the employer and the employee on behalf of the employee. He continued:

> And so, what you're saying is that at this point, that 5 percent would add to the ... percentage that the employee that is actively working currently pays. And if my numbers serve me correctly, ... it's about 8.69 percent, as I recall, so this would bring it up to ... 13 [percent]?

10:16:34 AM

REPRESENTATIVE KELLY answered that's correct.

REPRESENTATIVE ROSES continued:

> So, that's this pool of money for the active employees. The only way any money gets into this other pool over here - ... [regarding] the ones that are drawing benefits - is at the time they retire, the money moves from the active pool over to the inactive or the retired pool where the benefits are drawn from. Is that correct?

REPRESENTATIVE KELLY said that's roughly correct.

REPRESENTATIVE ROSES continued:

> And at the time that money is transferred, there's an actuarial calculation made for each of the those employees that retires, and that actuarial calculation is based on the average of their highest three years or whatever system they're in, and along with that [go] all the actuarial tables that determine longevity, ... et cetera. So, [what] goes with that, then, is the cost of the medical retirement system for whichever plan they fall under. And that amount of money is transferred to this inactive or retired pool.

REPRESENTATIVE KELLY confirmed that's correct.

REPRESENTATIVE ROSES continued: "So, we've defined where the 5 percent would be; it would be in the active pool. Where would the 80/20 split for the unfunded liability ... go?"

REPRESENTATIVE KELLY answered:

> That split would go to fill the hole between the 60 percent funding and 100 percent funding, which is the present value of those benefits over time. So, it goes into that bucket or into the past service cost bucket.

REPRESENTATIVE ROSES asked, "So, it goes into the retired one?"

REPRESENTATIVE KELLY answered yes.

REPRESENTATIVE ROSES said the ARM Board has a pool of money which it invests to generate revenue. He said the pool of money to pay retirees is not fully funded because of unanticipated costs and increased costs of medical, for example. Regarding the pool of money for active employees, he deduced, "They're not drawing benefits, so there's isn't shorted." He indicated that when those in that group retire, there will be an unfunded liability because there wasn't enough money generated into the system. He continued:

> So, there's an unfunded liability here and there's an unfunded liability here. That unfunded liability and the payments for those are the responsibility of the ARM Board. So, do we have a third pool of money, or does the ARM Board money sit entirely over here with the retired side?

10:18:10 AM

REPRESENTATIVE KELLY explained:

> The accounts established here reside in the Department of Revenue, but ... it is the responsibility of the ARM Board to determine what comes in the front end and what goes out the back, ... and to manage the money in the middle.

10:18:37 AM

REPRESENTATIVE ROSES said the Department of Revenue is responsible of all kinds of accounts, one of which is the ARM Board. He clarified that he wants to know where the 80/20 would go.

10:19:18 AM

REPRESENTATIVE KELLY said the 80/20 formula would be used to restore the unfunded liability.

REPRESENTATIVE ROSES summarized that the more that goes into the system, the more it will defer any increases to the unfunded liability. He said, "I think what I hear you saying is: The 80/20 is to address what we already know is the unfunded liability; the increase in the 5 percent is to help offset any additional increases to what that liability would be as the cost of doing business."

REPRESENTATIVE KELLY responded that that is essentially correct. He indicated that the unfunded liability is in a constant state of flux. For example, the next actuarial change relative to life expectancies will "put another hit on the system."

10:22:00 AM

REPRESENTATIVE GRUENBERG asked, "The 5 percent could go into either pot. Is that correct?"

10:22:26 AM

REPRESENTATIVE KELLY responded that it is clear there would be a problem with the 5 percent going into the unfunded liability pot, because that is a result of mistakes made in the past; therefore, it has to go towards offsetting the cost of the current period.

REPRESENTATIVE GRUENBERG noted that the House Special Committee on Ways and Means calls the two factors the "reserve account" and the "active account. He said there is another aspect to the issue, as well. He offered his understanding that the 5 percent would apply to both the defined benefit (DB) plan and the defined contribution (DC) plan.

REPRESENTATIVE KELLY clarified that that is actually not the case; [the 5 percent] applies only to the PERS' and TRS' DB plans.

10:26:37 AM

REPRESENTATIVE KELLY, in response to Representative Gruenberg, defined anticipated cost as the normal cost rate - the payment of benefits accruing to employees in the current period. He stated, "It does not relate to the period behind you. Nor does it relate to those who came in under the defined contribution plan."

10:27:29 AM

REPRESENTATIVE GRUENBERG observed that in a DC plan, the employee and the state employer each contribute a set amount, thus he questioned what unanticipated cost there would be.

REPRESENTATIVE KELLY indicated that comparing the DC and DB plans is like comparing apples to oranges. He reiterated that the discussion [about the 5 percent] is strictly about the DB plan.

REPRESENTATIVE GRUENBERG concluded, "So these people are paying an additional 5 percent to cover unfunded costs for somebody else."

CHAIR LYNN noted that that had been his previous question.

REPRESENTATIVE KELLY explained that the active employees in the current period are paying those costs that are accruing to them for future periods. The unfunded liability, he explained, relates to the DB plan and affects the people in that plan. He said, "We don't ask the retired folks to come to the table on this, because they are no longer in their productive period." He relayed that there are many people receiving benefits, and the cost of that coverage has gone up dramatically. Representative Kelly said what he is attempting to do - as much as he would like not to have to - is ensure that the very people who benefit and who are still actively employed help with the overall cost. He talked about bringing all parties to the table. He noted that in the past, about half the cost of benefits was paid by all the beneficiaries; however, that number has slipped to one-sixth. Representative Kelly said he thinks his proposal is reasonable, and he said he would even encourage unions to become involved. He concluded, "And so, the only place that's available - and it might even be difficult - is in the current cost rate, not in the unfunded liability portion. You can't mix the two."

10:33:06 AM

REPRESENTATIVE COGHILL said it seems that HB 179 would ask for an extra 5 percent from active employees to contribute to their own retirement. He indicated that he thinks the 80/20 requirement of the bill is problematic. He said the state has promised to have a retirement system. He stated, "So, at the end of the day, we could end up with 100 percent of the cost." He said employees agreed to pay a certain rate toward funding the retirement of their employees, while those employees have also agreed to pay into their own retirement. He offered his understanding that "that has ... been different from employer to employer." He continued:

> So, help me if I'm misunderstanding this, but the 80/20 that you have here, or the other numbers that are figured on how to blend that, is to say there's going to be winners and losers here, because some people have contributed very well, and are very sound, and are not contributing up to the 20 percent as employers. There are others who have not done so well, and we're going to end up picking up a big chunk of theirs.
>
> So, I guess what I'm asking is: [Is] the 80 percent really our responsibility, or do they really in fact bear 100 percent of the responsibility, and we're actually going in saying, "No, we'll pick that up," because we know at the end of the day it's a state full faith and credit issue?

10:35:31 AM

REPRESENTATIVE KELLY clarified that TRS has a single rate; PERS has 160 different rates - one for each employer. He said he thinks Representative Coghill's comment regarding the state's bottom-line responsibility is noteworthy. He said HB 179 is not the only option to consider, but it is one that "just might work." He said he has been chastised as a conservative for "putting the state numbers so high." He remarked that municipalities would think the number is too low; they want 85/15. Regarding municipalities, he related a story of Fairbanks selling its utilities. Regarding that story, he concluded:

> They did things which they thought at the time were responsible for the most part, as did the employees

> who were involved. So, I'm not saying that there isn't a tale of woe behind almost every place you point your finger, but I'm saying that this tries to cut through that, not have the law suits, [and] get all three of the parties to the table in a fair manner ....

10:39:50 AM

REPRESENTATIVE ROSES asked Representative Kelly to confirm that the aforementioned 5 percent would pertain only to the DB plan, which includes Tiers I, II, and III of [PERS] and Tiers I and II of TRS.

REPRESENTATIVE KELLY said that's correct.

REPRESENTATIVE ROSES directed attention to a chart on the third page of a memorandum in the committee packet from Senator Kim Elton, [which shows normal cost and accrued liability]. He illustrated that the PERS total for the Tier 3 DB plan, shown on the chart to be 10.83 percent, would increase with the addition of 5 percent.

REPRESENTATIVE KELLY first said the total obligation of the current period does not change, but then amended his response to say that it does, however, "ramp up." He referred to comments that he said Representative Roses had made on a previous day regarding cost-containment measures. Regarding the 5 percent, he used a 17 percent rate as an example. He said:

> Let's say that a year from now it's going to be 17 [percent]. That wouldn't change; that would not become 22 [percent]. ... For the employer, it would reduce that rate initially, and of course, over time, that is going up.

REPRESENTATIVE KELLY concluded that he thinks the answer to Representative Roses' question is no.

REPRESENTATIVE ROSES asked, "So, the increase to the employee does not show up in this normal cost that we have from Buck Consulting, when they're looking at what percentage is being paid in."

REPRESENTATIVE KELLY said the answer to that is yes. He continued:

> It would show up in this fashion: Let's say that today, just to pick up a number, ... the rate is 7 percent, by the employee, and that the total is 17 [percent]. So, the employer is picking up this ... extra ... 10 [percent]. If the employee steps up to the plate for 5 [percent], the 17 doesn't change, but the impact initially on the employer is to bring that total cost down.

REPRESENTATIVE ROSES calculated that with the 5 percent added, the employer normal cost would show an increase, though not the full 5 percent.

REPRESENTATIVE KELLY responded no. He explained:

> It would stay exactly the same, assuming there was no upward pressure at that moment you freeze it. Call it 17 [percent], the employee ... would be picking up a share that is currently in the employer's calculations, and that relieves some pressure on them, relative to this total cost.

10:43:18 AM

REPRESENTATIVE ROSES, regarding the proposed 80/20 split, remarked that only 1 of the 160 employees in PERS is the State of Alaska. The other 159 in that retirement system include school districts and the university system, for example. He emphasized that although they operate as separate entities, the vast majority of their operating expenses and funds come from general fund appropriations from the State of Alaska. He asked Representative Kelly if he thinks that is a fair assessment.

REPRESENTATIVE KELLY answered yes. He offered an example.

REPRESENTATIVE ROSES stated:

> The major gain we're going to have by doing an 80/20 split is really only going to have the net result on those communities that have their own taxation base to where they can pick up a portion of that 20 percent. Because [for] all of those school districts and all of those areas and all of those employers that get everything through a general fund, you can call it an 80/20 split if you want, but the state's paying 100 percent. So, the only ones we're really talking about are those entities that have some ... type of

individual revenue production other than general funds.

REPRESENTATIVE KELLY indicated that Representative Roses' statement is accurate.

REPRESENTATIVE ROSES remarked that the individuals representing the small pool [of entities with their own revenue production] are the same individuals who come to the offices of the legislature asking for increased revenue; therefore, he suggested, "Isn't the state also picking up a percentage of that?" He stated that he understands the significance of the issue and applauds Representative Kelly for tackling it. He said if the legislature does not find a fix, it will be holding up all the rest of the funding for every other entity that has not been addressed in the budget. He said, "The thing I'm having the hardest time dealing with is it appears to me to be a very small percentage of people that we're talking about that were even going to be able to pick up that 20 percent themselves. The state's really responsible for almost all of it."

10:47:25 AM

REPRESENTATIVE KELLY responded that "that number is identifiable." He said he does not disagree with what Representative Roses said. He described [the unfunded liability] as a complicated issue to solve. He said HB 179 is different than other approaches because it focuses on "how you split it up on the rate." He mentioned other proposed solutions. He concluded, "I've tried to pick the one area - that's the normal cost rate - we just might be able to agree upon."

10:50:55 AM

LARRY SEMMENS testified. He stated his appreciation of Representative Kelly's work on HB 179. He noted that he is the finance director at the City of Kenai and a member of the ARM Board. Last year, when Representative Roses was a member of the ARM Board, both short-term and long-term recommendations were sent to the legislature. The short-term solution was to put more money into the systems to halt the growth of the unfunded liability. The long-term solution was embodied in House Bill 375, a bill which passed unanimously. Mr. Semmens said Representative Kelly has inserted parts of House Bill 375 into HB 179, including the past service liability accounts and a split between the state and employers. He noted that in House Bill 375, that split was 85/15, and in HB 179 it is 80/20.

MR. SEMMENS said that from the standpoint of both municipal employers and the Alaska Municipal League (AML), priorities are stability, affordability, and predictability of the rates, and [HB 179], at 80/20, certainly addresses the issue of affordability. He noted that last year AML had a target rate of 20 percent. Using the 80/20 calculation to the current PERS rate of approximately 40 percent results in an approximate 20 percent rate for employers. Mr. Semmens stated he is confident that although AML's official position is 85/15, the 80/20 split would be endorsed after an official meeting with its membership. He concluded, "... If we can come up with a long-term stable rate ... in the neighborhood of 20 percent, I'm confident that employers will welcome that."

MR. SEMMENS said he has not studied the technical fixes recommended by the administration. He encouraged the committee to focus on the normal cost rate, which is rising. He said, "Employees may be willing to take a share of that."

10:54:51 AM

LYDIA GARCIA, Interim Executive Director, National Education Association of Alaska (NEA-Alaska), testified on behalf of the 13,000 members of NEA-Alaska in opposition to HB 179. She questioned why time is being spent on a bill that is not only unconstitutional, but also so wrong for the State of Alaska. She continued:

> Governor Sarah Palin has stated on numerous occasions that a pension is a promise. NEA-Alaska agrees with the governor that the state promised employees a specific pension for a specific contribution. It was not public school employees who decided to reduce the employer contribution early this decade. Why would the state want to put any liabilities on the backs of the employees? [Martin Luther] King was fond of saying, "A promise made is a debt unpaid." The State of Alaska made the promise to its employees; the state needs to pay the debt.

MS. GARCIA said HB 179 proposes to cut the pay of all public employees by 5 percent, which she said would affect every single public employee, including teachers, police officers, and firefighters. She stated that educators making $15,000-$20,000 a year can't afford to pay an additional $750-$1,000. She reminded the committee that NEA-Alaska, the Anchorage Education Association, and the Anchorage School District have recently finished up to two years of "intense, arduous bargaining." She continued:

> The raises of 3-4 percent over the next few years are fair and will hopefully keep inflation at bay. I shudder to think of the passage of HB 179 and telling our members that their 3 percent raise is actually a 2 percent cut in pay.

MS. GARCIA noted that two years ago, Chair Lynn was one of the leaders involved in the fight to maintain the defined benefit program for public employees. She emphasized the importance of returning Alaska to a defined benefit program for its public employees. She said there are several other pieces of legislation addressing the issues of retirement and the unfunded liability. She asked that the committee not allow HB 179 to pass out of the House State Affairs Standing Committee.

MS. GARCIA, in response to Chair Lynn's request that she explain why HB 179 is unconstitutional, cited Article 12, Section 7, of the Constitution of the State of Alaska, which read as follows [original punctuation provided]:

> SECTION 7. Retirement Systems.Membership in employee retirement systems of the State or its political subdivisions shall constitute a contractual relationship. Accrued benefits of these systems shall not be diminished or impaired.

10:59:29 AM

REPRESENTATIVE GRUENBERG observed that HB 179 includes many types of legal issues; however, neither it nor any of the other pension legislation is slated to be heard in the House Judiciary Standing Committee. He noted that three of the members of the House State Affairs Standing Committee also sit on the House Judiciary Standing Committee, and he emphasized the importance of considering all the legal issues related to HB 179. To all those who had testified or were yet to testify, he stressed the necessity of legal opinions and case citations to back up statements. He said without such documentation those statements would not be helpful to the committee. He said he is not just talking about Article XII, Section 7, but is also referring to other issues, such as the impairments of collectively bargained contracts.

11:01:06 AM

CHAIR LYNN confirmed that he did oppose Senate Bill 141 last year. He said he wished that a bill such as HB 179 had been available then. He talked about the balance of extricating the state from the unfunded liability while simultaneously protecting the rights of the workers. Employees and retirees must be the bottom line in the issue, he posited.

11:02:19 AM

MS. GARCIA, in response to Representative Gruenberg, said she would be happy to provide the legal opinions and information related to her statements.

11:02:52 AM

ROD L. BETIT, President/CEO, Alaska State Hospital and Nursing Home Association (ASHNHA), noted that he is representing 37 member facilities from around the state. He noted that most of those facility representatives were in town the previous day for a legislative update. He continued as follows:

> [They] took up this piece of legislation and asked that I report to you that they greatly appreciate Representative Kelly bringing this piece of legislation forward to deal with the piece on unfunded liability between the state and employer funding of that ... hole. They understand that hole has to be filled, but they've in good faith participated at rates that they felt were appropriate for those years.
>
> The difference between the 35 or 40 percent rate and the 20 percent is just astronomical on our members, particularly our five, small hospital members that are also community hospitals. Petersburg, for example: the difference would be $800,000 a year - not just one year, but we're told for the next quarter of a century - to dig out of this hole. They have a patient census of 1.5 patients per day. The rate increase to come up with that kind of money would just be enormous - in the 40-50 percent range.

> I would ask that this be given consideration and that you do give support to the 80/20 split. We think it's a fair way to try to recover from the damage of the past and to spread that burden in a more (indisc. -- sneezing) way, but in a way that's sustainable for the employers that are ... contributing to this problem.

11:04:50 AM

REPRESENTATIVE GRUENBERG stated that the committee also needs legal research regarding "the interplay between this legislation and any applicable federal legislation." He asked Mr. Betit to comment.

MR. BETIT responded that ASHNHA is not speaking to any legal aspect of HB 179, nor is he speaking to any components that deal with employee contributions to the current Public Employees' and Teachers' Retirement Systems. He clarified that he is speaking solely to the policy question of how much of the past ills - the unfunded liability - should be borne by the state and how much by the employer.

11:06:01 AM

GAVIN D. CHARRIER testified on behalf of himself and the Local 6137 Alaska Public Employees Association/American Federation of Teachers (APEA/AFT). He relayed that he is a 34-year resident of Alaska who has been employed by the Ketchikan Gateway Borough as an airport equipment mechanic and aircraft rescue firefighter, contributing 7.5 percent to PERS. He continued:

> As a 19-year collective bargaining negotiator for our employee group, Local 6137 of the [Alaska Public Employees' Association/American Federation of Teachers (APEA/AFT)], historically Ketchikan is noted as being one of the highest cost of living regions, while also being the lowest political ... subdivision in the state. Over the years our members have suffered substandard wages in lieu of a generous benefit package that we have collectively been able to maintain through negotiations with the Ketchikan Gateway Borough.
>
> PERS/TRS retirement is considered to be one of those benefits that is under constant erosion, such as Tier I, II, III, IV, and now a proposed increase in contribution rates, with nothing more other than

> status quo in return. If employee contribution rates are successfully increased to 5 percent from the current 9.6 school district, 7.5 police/firefighters, and 6.75 of all others, to a 14.6, 12.5, and 11.75 percent, respectively, then this will certainly create a financial hardship for many of those current substandard ... wages barely enough to make ends meet.
>
> PERS/TRS employees have had no option but to contribute every pay period to their retirement account. The explanation that I've been given is that the employer, on the other hand, doesn't have to contribute a plug nickel into the Tier I, II, or III employees' account until the day comes when that particular employee retires and starts drawing their hard-earned retirement at the PERS Board designation's percentage amount calculated at 2 percent for ... their first ten years of employment, plus 2.5 percent per year for all years after ten, times the average of the three highest consecutive years of salary.
>
> With the creation of Tier IV employees last year, there is no new money coming in to help offset the deficit retirement account balance. When the retiree draws their monthly retirement check from ... PERS, PERS sends simultaneously [to] the employer their portion of what they owe the account to proportionally refund that retirees' retirement at what has already been determined by the PERS Board as previously mentioned.
>
> ... I believe it's time for the employers to ... take fiduciary responsibility, step up to the plate, and begin actively participating in matched funding PERS/TRS Tiers I, II, and III defined benefit groups upfront, alongside the employees' contributions bi-monthly as ... they currently are with the newly created Tier IV defined [contribution] employee group.

11:09:32 AM

REPRESENTATIVE ROSES asked Mr. Charrier to confirm his indication that school districts and municipalities don't pay anything into the system until the employee retires.

MR. CHARRIER said that has been his understanding after phone calls to representatives of PERS. He said he knows there are different political subdivisions of the state that fund the account readily and generously, while others seem to postpone their payments into that account until the employee retires.

REPRESENTATIVE ROSES suggested the possibility that two issues are being mixed together in this discussion. He clarified:

> There's an account that is for the active employees, where the employee and the employer pay into that account. Then when that employee retires, the money and all of the obligation that goes with that retirement then transfers from that active account into the retired account. So, what you're referring to, I think, is the process by which the active funds move over to the retired or the inactive funds. But the municipalities pay it in each month the same as the employee does; it's into that active account rather than the retired account. So, I think what you're stating is partially correct, but the municipalities and school districts pay in every month [the] same as everybody else does - it just doesn't move to that account with the employee until they retire, but the money's already there.

11:11:36 AM

JIM DUNCAN, Business Manager, Alaska State Employees Association Local 52, on behalf of the approximately 8,200 general government unit employees in Alaska, testified in opposition to the provisions of HB 179 related to the increase in employee contribution of 5 percent. He said he opposes the increase both for PERS and TRS employees, even though he does not represent the latter. He stated that that provision is unconstitutional. He discussed an attorney general's opinion on the matter, written in April 2005, [included in the committee packet], which outlines that there is a requirement in the constitution that makes it unlawful to impair benefits of the retirement system once someone has entered into that system. He related that there have been six court cases on the issue, to date, and the court has found for the employee each time.

MR. DUNCAN said back in 1986, when he was a Representative in the House, the employee contribution rate did increase; however, that happened at the same time as an enhancement of benefit - the automatic pension adjustment. He said if the committee moves forward with the bill, he would expect litigation.

MR. DUNCAN reviewed that House Bill 475 was introduced last year, which included "fix it" provisions for the already passed Senate Bill 141; however, House Bill 475 never made it through the Senate and emergency regulations had to be adopted as a result. He stated:

> And based upon information provided to the [Internal Revenue Service (IRS)] that legislation had passed, the IRS found the defined contribution plan to be compliant. The provisions were never passed; they were put into place by emergency regulation. It is my position that it was not appropriate to do that by emergency regulation, and so, whether or not the provisions are in place ... is still subject to challenge."

MR. DUNCAN suggested that if the committee wants a solution to the retirement and benefits system, it should return to the Tier III defined benefit plan. He concluded, "The Buck Report shows that the Tier III defined benefit plan is not causing a problem, is not really causing an undervaluation. In fact, it is the same cost if not less costly than the defined contribution plan."

11:15:46 AM

CHAIR LYNN asked Mr. Duncan what he would think of HB 179 if the 5 percent provision were not in it.

MR. DUNCAN replied that the Alaska State Employees Association stands ready to assist the legislature in making its policy call as to whether the split should be 80/20 or 85/15, but he noted that his preference is for the latter.

11:16:57 AM

REPRESENTATIVE GRUENBERG directed attention to a memorandum from Legislative Legal and Research Services, dated January 29, 2005, [included in the committee packet], which he pointed out only refers to a 1981 case. He requested that Mr. Duncan have his legal staff review the memorandum and respond to it. Furthermore, he said he looks forward to getting a legal memorandum from Mr. Duncan. Finally, he said he is concerned about the effect of the 5 percent change on currently existing collectively bargained agreements.

MR. DUNCAN stated that although he has great respect for the attorneys who work in Legislative Legal and Research Services, the legislative counsel who wrote the January 29 memorandum is "absolutely wrong in that memo" and "did not give full consideration to the provisions that are referenced in the attorney general's opinion." In response to Representative Gruenberg's third statement, he said it is clear that a 5 percent increase in an employee's contribution rate equals a 5 percent decrease in pay. He stated, "We are trying to negotiate a collective bargaining agreement for this point, but have not yet reached an agreement. We hope to in the near future." Mr. Duncan said over the past 10-15 years, employees have seen their take home decrease, because the wages of state employees have fallen 17 percent behind the increases in the consumer price index (CPI). Conversely, the federal government and private sector has kept pace [with the CPI].

11:19:34 AM

MICHAEL E. LAMB, CPA, CGFM, Chief Financial Officer, Fairbanks North Star Borough, noted that he is a co-chair of the AML revenue finance subcommittee. He thanked Representative Kelly for his "tenacity and dogged determination to help in crafting a final solution to the multiple PERS and TRS issues." He said the proposed legislation includes some necessary components. He said he thinks the following needs to be combined to come up with a solution that would work long term and would embrace the previously mentioned components of predictability, stability, and affordability: some of the language from HB 179, some of the governor's cost-sharing language, some of the DB/DC salary-base language, some of House Bill 13's pension obligation bond language - also supported by the governor, and some of the House committee substitute proposals.

MR. LAMB stated that HB 179 recognizes the need for technical corrections made as a result of Senate Bill 141. Furthermore, it recognizes the existence of a consolidated cost-sharing system and the need for legislative language that "reflects that." He spoke of "an outcome where all member employers should be assigned a single, uniform rate," and he said that should include the State of Alaska as employer. He said there must be a rate that is predictable and palatable to everyone's budget.

MR. LAMB emphasized that the aforementioned 85/15 split was intended so that 85 percent of the bill was "pulled away" and "treated like a mortgage payment," with the balance of the liability - the 15 percent - shared "across all member employers, including the state," so that the state's budget also had a benefit rate that was affordable. He said the 80/20 split proposed in HB 179 is not quite structured like the "80/15 shared solution." "Accordingly," he said, "the resulting member employer rates end up too high after known, future-year, unfunded obligation increases are factored in."

11:23:58 AM

MR. LAMB, in response to a request for clarification from Representative Coghill, emphasized that the key element in this discussion is about the rate, which he said has to be affordable. He stated, "If the rates in the past had been set appropriately, ... the only rate that we would be talking about today is the normal cost rate, which is 14.48 [percent] for [fiscal year 2008 (FY 08)]." He said he thinks many people are saying that the state is "bailing out in helping other member employers pay for their unfunded obligation." Mr. Lamb offered his perspective that it is those member employers - with every dollar paid above the 14.48 percent normal cost rate - who are actually helping pay down the obligation that was created by the state's setting rates incorrectly in the past. He concurred with Representative Roses that the State of Alaska's budget is the source of funding not only for its own employees, but also for the University of Alaska and school districts - especially rural schools. The goal, he said, needs to be to find a rate whereby all member employers pay as much as they can, so that services are provided, without going bankrupt.

11:27:55 AM

DUANE MORAN, President, Anchorage Council of Education, which is affiliated with the Alaska Public Employees' Association/American Federation of Teachers, noted that he is a PERS Tier III employee. He expressed appreciation for Representative Kelly's efforts in introducing HB 179, but said he takes significant issue with the portion of the bill which proposes a [5 percent] increase in employee contributions. He asked the committee to consider the law of unintended consequences: A 5 percent, after-tax cut in wages would result in an unintended movement from the active employee pool to the retired pool. The $10 billion short-funding is over a 20- to 25-year period, he said. He indicated that a rapid increase in current costs will also increase the liability. He agreed that predictability and certainty are important in labor negotiations, because, "If there's a change this year on the employee contribution, what's to say there wouldn't be a change next year?" Mr. Duran concluded:

> There's a difference between having skin in the game and a pound of flesh, and a 5 percent, after-tax pay cut would be more than a pound of flesh.

11:30:35 AM

REPRESENTATIVE GRUENBERG asked if a 5 percent deduction would have the same effect as a 5 percent tax on employees.

MR. DURAN answered, "Absolutely." He revealed that many employees have said they are at the point where if they were faced with a 5 percent cut in wages, they would leave state employment, work for the private sector, and collect the insurance benefits of their pension now rather than in four to five years. He mentioned HB 191, which proposes a $1,500 bonus for employees currently eligible to retire to continue working, while HB 179, he observed, would cut salaries by 5 percent. He questioned what message the legislature is trying to send.

11:31:56 AM

REPRESENTATIVE ROSES offered the following point of clarification:

> I think I heard in your testimony that this would be a 5 percent after-tax deduction, but ... actually, the way it's proposed, it's a 5 percent prior to tax. So, ... the net result is not a 5 percent decrease in pay. It would be more like two and three-quarters to three and a quarter, depending on a person's wage. But nonetheless, the impact that you're talking about would be ... [that] take home pay would be reduced.

MR. DURAN recollected that he had heard the term 5 percent "after-tax" during Representative Kelly's testimony.

11:32:39 AM

REPRESENTATIVE COGHILL, responding to Mr. Duran's previous statement regarding a pound flesh, asked him to think about the "$10 billion tax that's going to be sent to the people of Alaska to keep your retirement whole." He asked that Mr. Duran "put that in balance."

MR. DURAN remarked that he does not think any of the current members of the legislature were a part of the decision-making processes in the 1960s. He said mistakes were made by "a lot of different groups of people," but "employees did not have that contribution to those mistakes."

REPRESENTATIVE COGHILL responded, "We could argue about it, but the fact is: neither did the children who are going to pick this bill up."

CHAIR LYNN disclosed that he has a son and daughter-and-law who are under TRS in Anchorage.

REPRESENTATIVE COGHILL said everybody on the committee probably has some [relatives in PERS and/or TRS].

11:34:35 AM

RICK SCHIKORA, testifying on behalf of himself, said he thinks Representative Kelly is doing a good thing by attempting to "get everybody to come to the table." He said it sounds like the 80/20 split may work. If Mr. Duncan is correct that the proposed 5 percent increase is unconstitutional, he said, then perhaps there are other options. He said DB consultants have told him one option is to "change the go-forward rate of the multiplier." He offered further details.

11:37:14 AM

GARY HUTCHINSON, testifying on behalf of himself, told the committee that he has six years' experience as a public official for his local municipality and understands the impact that the unfunded liability has had on his school district and local borough. He thanked Representative Kelly for his efforts. He stated, "I have trouble understanding how in the world we can reach into any savings account that belongs to all Alaskans and take $8 billion out to fund this pension plan that we cannot afford, without fixing it prospectively." He said some of the ideas of "the prior speaker" are "in the right direction." He continued:

> Certainly I understand [Representative] Kelly's interest in increasing the employee contribution to buy another 5 percent is designed to try and mitigate the fact that the plan would not be fixed under this scenario, and that there would be accruing unfunded liabilities, and that the 5 percent is designed to be

> directed toward that. That is a step in the right direction, but I think we need to also step back, look at this plan that is auguring into the savings accounts of all Alaskans at an alarming rate, and ask ourselves, "Is this a pension plan that we can afford in the future?"

MR. HUTCHISON said when he served in public office two years ago, the deficiency then was $5.7 billion, and he said it is stunning that it is currently measured at $10 billion. He stated:

> I am not in favor of the 80 percent bail out if there is not some adjustment to the plan so that prospectively there isn't additional, unfunded amounts accruing to the tax payers. I'd be more in favor of 65 percent, or lower, as the governor's proposed.

11:39:42 AM

REPRESENTATIVE GRUENBERG noted that some municipalities have limited their taxes so much that they are not contributing as much as some of the other municipalities, and he said, "We're trying to do a one-size-fits-all for municipal contributions." He asked Mr. Hutchinson how the state should handle that situation.

MR. HUTCHINSON said he is not currently an official. Notwithstanding that, he expressed his own opinion favoring a cost-sharing approach, which he said treats PERS more like TRS. He said, "That's a fair way of dealing with this plan, and I think it would be more politically palatable." He surmised that Representative Gruenberg is probably referring to rural areas that don't contribute, ultimately resulting in the state's picking up the tab "one way or the other." He said the issue needs to be about fixing the state's retirement plan. He stated:

> It would be better to have more costs ... flow through to the municipalities and the tax payers if no adjustment to this plan occurs, making it a more affordable plan prospectively, because the higher cost that would trickle down to the municipalities, trickle down to the tax payers, would be a means of educating the general public of the severity of this problem.

11:42:30 AM

JASON AVERY, testifying on behalf of himself, said he is a member of the Alaska Public Employees Association and works for Fairbanks North Star Borough Parks and Recreation Department. He said he is a PERS Tier III employee and has worked for the borough for 10 years. He stated:

> I understood when I graduated from college that as a public employee, I'd probably be making less money than I would be in the private sector, but would have more stable benefits and a decent retirement to look forward to. I'm proud of what I do, but with each year I feel the public employees are falling farther and farther behind in the pay that we receive and the retirement benefits we were promised. I support statutory changes that will protect employers from having to pay ever increasingly unsustainable rates to the retirement system, and I understand that leaving the current system as it is will cause great harm to Alaska's schools and local governments.
>
> I believe that the state is responsible for paying at least 80 percent of the unfunded liability, as it's the state's responsibility for the mistakes made by the investment in actuarial companies that [it] hired, and that the remaining 20 percent be covered by the employer. I do not believe that the public employees of this state should be expected to pay an additional 5 percent of their hard-earned paychecks to pay for mistakes that they did not make. Furthermore, I feel that the so-called fix of creating a Tier IV with [Senate Bill] 141 has made it very difficult to recruit qualified, new employees, and gives no real incentive for those employees to stay in the State of Alaska as a defined benefit system has in the past.

11:45:00 AM

DAN WAYNE, Attorney, Legislative Legal and Research Services, as the attorney assigned to HB 179, and in response to Chair Lynn and Representative Gruenberg, said there may be a constitutional issue with the proposed 5 percent increase. In response to a follow-up question from Representative Gruenberg, he said he does not have a copy of the legal opinion to which Mr. Duncan previously alluded.

REPRESENTATIVE GRUENBERG said he would like Mr. Wayne's opinion regarding the aforementioned legal opinion in the committee packet and the attorney general's opinion, once Mr. Wayne has had a chance to read both.

11:46:12 AM

REPRESENTATIVE KELLY, regarding the legality of the bill, said he is aware of the challenge relative to the past service rate. The opinions of Legislative Legal and Research Services and the attorney general address the normal cost rate, which is the current period. He said some say the reported $10 billion unfunded liability is actually closer to being $12 billion. He warned that the state's retirement system could cost $900 million a year for the next 25 years before being solved. He emphasized the enormity of the problem which the state faces. He said he met with the new attorney general [Talis Colberg], who is aware of HB 179 and has questions to answer for the sponsor. He concluded, "Hopefully we can find a way to make sure that everyone's trying to lift their fare share."

11:48:25 AM

CHAIR LYNN stated concern over the potential unconstitutionality of the proposed 5 percent provision. He said there may be battling opinions between the previous attorney general and the current one.

REPRESENTATIVE KELLY said he intends to get answers to the constitutional question, but it is not his intention to "drop the plan to bring all three players to the table."

11:49:39 AM

REPRESENTATIVE KELLY, in response to a question from Representative Gruenberg, said he hopes that Attorney General Colberg can be forthcoming with an answer regarding the question of constitutionality.

11:50:32 AM

REPRESENTATIVE ROSES stated:

> If I've led anybody to believe that I have all the answers to these questions, I've certainly misdirected people, because I don't have all the answers; I don't even know all the questions. All I know is that we

> have serious issue to deal with and we have to get a handle on it right away or that [$12 billion] will be [$15 billion].
>
> ... One of the comments that somebody online made is: "You know, when I looked at it a few years ago, it was $2.5 billion and now it's [$10 billion]. How did you get to that point?" Well, it's simple: we didn't address the problem. And if we don't address the problem now, it's only going to get worse.

REPRESENTATIVE ROSES expressed appreciation of Representative Kelly's willingness to bring something for the committee to consider. He recognized that any proposed legislation will offer parts that people like and other parts that are not liked.

REPRESENTATIVE ROSES said there are two parts of the bill that concern him: First the proposed 5 percent increase in employee contributions. He said he will not talk about the legal issue, but wants to talk about the standpoint of what the 5 percent does:

> The only responsibility I see that the employee has in this is the fact that through their different negotiations they've gotten salary increases, and as a result of those salary increases, they have a higher retirement. I've heard some people say, "Well, they've negotiated themselves some very fine medical benefits." Well, that's not true. The medical benefits they have now [have] nothing to do with this. The medical benefit that adds to the unfunded liability is the medical benefit they would get when they retire; it has nothing to do with the active medical benefit. So, people need to understand that: that's got nothing to do with the state - that's everything to do with their local negotiations process.
>
> So, the only real part that the [employees have] played in this is the desire to have an increase in their wages. The serious problem I have with the 5 percent: it almost in some ways becomes retroactive, even though there's an effective date that takes it forward. And the reason I say it becomes retroactive is: anyone that has signed a negotiated agreement for salaries - ... three-year contracts - ... can't change those. Had they known before they signed that

contract and negotiated that contract that there was potential for a 5 percent additional employee contribution that they had to make, they maybe would have negotiated differently, because that's really the only part that the employee has any control over. Everything else is controlled by the state: where the ARM Board sets the rate; whether the legislature funds the rate; whether they decide, when the actuary says, "You need to pay 7 percent," and we decided we're only going to pay 5, the actuary said, "You need to pay 11, we decided to only pay 5." That ARM Board is [a] ... quasi employee of the state.

And so, clearly, the major responsibility of where we are is the stakes, regardless of how we got there - and [there are] 47 different versions. But the 5 percent seems to me to be the one that we do have some control over right now. And I don't want to sit here and debate this thing for six weeks and try to kill it in committee, because the fact of the matter is we've got six other bills out there that are dealing with the same issue. And they're all going to be consolidated in the [House] Finance Committee. The Senate's going to do the same thing, and then we're going to have to ... form a group that's going to look at trying to solve the issues between the two. But I have a very hard time moving this thing forward. And I'll debate the 80/20 when it gets somewhere else - maybe even on the [House] floor - if it ends up in that version. But the 5 percent is the one that I'm having the most concern with, as well as the legal part, because I think it's a little excessive, and I'll tell you why:

... If I get overridden on this, and everybody else thinks that this is a good thing, I would like to see it ... instituted in a progressive manner, so that we start out with something that's a little more manageable - [for example] if it were a 2 percent and then it went to 3.5 percent, and then it went to 5 percent, or, even if we didn't do anything with it, if we passed it at the 5 percent, put the effective date on the 5 percent at least three years out, because nobody has a contract that lasts more than three years - so the people at least knew where they were going to be when they were negotiating their salaries, instead of making it retroactive to something they have ... no capability of changing.

REPRESENTATIVE ROSES asked Representative Kelly for his response.

11:55:43 AM

REPRESENTATIVE KELLY said he does not disagree with Representative Roses. He said everyone is working hard on this issue. He said he thinks "these things" will sort out "as we go forward." He offered an example of a situation when everybody came to the table to solve a problem. He said there are Alaskans who are not at the negotiating table and he is trying to represent them. He agreed that the employees have done nothing wrong, and he stated that he is not trying to pick on them. He said it is the legislature that sets the percentages. He relayed that he would like to see all people involved lifting their fair share.

12:00:03 PM

CHAIR LYNN offered his understanding that the amount of the percentage does not make a difference in whether or not it is unconstitutional.

REPRESENTATIVE KELLY said that is "right on target." He asked, "Is it not a significant enhancement to the plan to take both of them from 60 and 65 percent funding to 100 percent health and full funding? ... I would submit that that is an enhancement and that the court might just take a look at that." Representative Kelly pointed out that the current benefits were established long before a variety of medical innovations became available that also increased the cost of health care benefits, and the rates have remained unchanged.

CHAIR LYNN remarked that the court system is unpredictable.

12:02:18 PM

REPRESENTATIVE ROSES said the most predictable part of the unfunded liability is related to the pension, and he agreed that the most unpredictable part is related to the cost of medical benefits. He said he knows the bill needs to be advanced, but he said he is likely to offer an amendment for a graduated employee contribution increase, as well as an amendment to postpone "the application of that process for three years out so that any existing contracts that just got negotiated ... won't be affected." He noted that delaying the 5 percent would cause an increase in the unfunded liability, but that impact would be minimal compared to the potential negative impacts.

12:04:56 PM

REPRESENTATIVE KELLY said the money that the employees would bring to the system would be $100 million a year. He said he would not debate Representative Rose's amendments out of respect for the committee.

12:05:13 PM

REPRESENTATIVE LYNN closed public testimony. He expressed appreciation of Representative Kelly's eloquence and his tackling of the matter.

12:05:40 PM

REPRESENTATIVE GRUENBERG said he had to leave, but did not want to miss voting on this issue.

12:06:04 PM

REPRESENTATIVE ROSES requested holding the bill until [Tuesday's] meeting.

12:07:08 PM

REPRESENTATIVE DOLL expressed her appreciation of Representative Roses' input on the bill, as both a former math teacher and former member of the ARM Board, and she stated support of his request to hold the bill.

12:07:38 PM

REPRESENTATIVE COGHILL said he was prepared to make a motion to move the bill out of committee. He stated his concern regarding holding the bill in the House State Affairs Standing Committee is that it could slow down the conversation in the House Finance Committee. He said he would be "game" to hold the bill to the next week as long as no political games are being played.

CHAIR LYNN said he will not allow any political games to be played concerning this or any other bill heard in the House State Affairs Standing Committee. Furthermore, he stated his intent to hear HB 179 first thing at the committee's next meeting.

12:09:22 PM

REPRESENTATIVE ROSES said he would be willing to move his own bill back that's slated for Tuesday's schedule if that would help.

12:09:52 PM

CHAIR LYNN announced that HB 179 was heard and held.

ADJOURNMENT

There being no further business before the committee, the House State Affairs Standing Committee meeting was adjourned at 12:10:43 PM.