

**ALASKA STATE LEGISLATURE
HOUSE SPECIAL COMMITTEE ON WAYS AND MEANS**

April 11, 2007

7:14 a.m.

MEMBERS PRESENT

Representative Mike Hawker, Chair
Representative Anna Fairclough, Vice Chair
Representative Bob Roses
Representative Paul Seaton
Representative Peggy Wilson
Representative Sharon Cissna
Representative Max Gruenberg

MEMBERS ABSENT

All members present

OTHER LEGISLATORS PRESENT

Representative Mike Kelly

COMMITTEE CALENDAR

HOUSE BILL NO. 206

"An Act relating to the accounting and payment of contributions under the defined benefit plan of the Public Employees' Retirement System of Alaska, to calculations of contributions under that defined benefit plan, and to participation in, and termination of and amendments to participation in, that defined benefit plan; making conforming amendments; and providing for an effective date."

- MOVED CSHB 206 (W&M) OUT OF COMMITTEE

HOUSE JOINT RESOLUTION NO. 5

Proposing amendments to the Constitution of the State of Alaska limiting appropriations from certain mineral revenue, relating to the balanced budget account, and relating to an appropriation limit.

- SCHEDULED BUT NOT HEARD

PREVIOUS COMMITTEE ACTION

BILL: HB 206

SHORT TITLE: PERS CONTRIBUTIONS; UNFUNDED LIABILITY
SPONSOR(s): RULES BY REQUEST OF THE GOVERNOR

03/16/07	(H)	READ THE FIRST TIME - REFERRALS
03/16/07	(H)	W&M, FIN
03/28/07	(H)	W&M AT 7:00 AM HOUSE FINANCE 519
03/28/07	(H)	Scheduled But Not Heard
03/30/07	(H)	W&M AT 7:00 AM HOUSE FINANCE 519
03/30/07	(H)	Heard & Held
03/30/07	(H)	MINUTE(W&M)
04/02/07	(H)	W&M AT 7:00 AM HOUSE FINANCE 519
04/02/07	(H)	Heard & Held
04/02/07	(H)	MINUTE(W&M)
04/04/07	(H)	W&M AT 7:00 AM HOUSE FINANCE 519
04/04/07	(H)	Heard & Held
04/04/07	(H)	MINUTE(W&M)
04/11/07	(H)	W&M AT 7:00 AM HOUSE FINANCE 519

WITNESS REGISTER

ANNETTE KREITZER, Commissioner Designee
Department of Administration(DOA)
Juneau, Alaska
POSITION STATEMENT: Answered questions regarding HB 206.

KATHLEEN LEA, Retirement Manager
Division of Retirement and Benefits (DRB)
Department of Administration (DOA)
Juneau, Alaska
POSITION STATEMENT: Answered questions on HB 206 and provided information on retirement and benefit issues.

ACTION NARRATIVE

CHAIR MIKE HAWKER called the House Special Committee on Ways and Means meeting to order at 7:14 AM. Present at the call to order were Representatives Hawker, Fairclough, Wilson, Roses, Seaton, and Gruenberg. Representative Cissna arrived as the meeting was in progress. Representative Kelly was also in attendance.

[7:14:39 AM](#)

HB 206-PERS CONTRIBUTIONS; UNFUNDED LIABILITY

CHAIR HAWKER announced that the first order of business would be HOUSE BILL NO. 206, "An Act relating to the accounting and payment of contributions under the defined benefit plan of the

Public Employees' Retirement System of Alaska, to calculations of contributions under that defined benefit plan, and to participation in, and termination of and amendments to participation in, that defined benefit plan; making conforming amendments; and providing for an effective date."

7:15:38 AM

REPRESENTATIVE SEATON opined that one of the chief components of a cost share system should be to structure a mechanism by which all employers are on "an equivalent basis" when they enter the system. He said he believes that the one-year hold harmless provision as currently proposed under HB 206 is not sufficient to keep some employers in the system. He suggested that fairness requires some kind of equity among employers as they enter a cost share arrangement. He referred to a document titled "Hold Harmless", dated April 10, 2007, which was provided to the committee. He reminded the committee that "there is no wording in [HB] 206 that provides the hold harmless." He suggested that his approach could be described in a letter of intent which could be sent to the House Finance Committee.

7:18:06 AM

CHAIR HAWKER asked whether Representative Seaton's approach could be considered a conceptual amendment to HB 206.

REPRESENTATIVE SEATON agreed that his suggested approach to the hold harmless issue could be considered a conceptual amendment to HB 206. He reiterated his belief that employers must be at an equivalent place when they enter the cost share pool. He opined that the current proposal to set employer contributions at approximately 32 percent will cause many employers to drop out of the system as it is much too high a rate. His proposal is based on information from the Alaska Municipal League (AML) and other entities that municipalities "could stand" an employer contribution rate of 22 percent. He went on to say that a 22 percent employer contribution rate is reasonable, while a rate as high as 31.86 percent is "unworkable." He suggested that to get to a rate of 22 percent, there will need to be a reduction in the unfunded actuarial accrued liability (UAAL), whether by pension obligation bond (POB), or other mechanism. He summarized that this approach establishes how much of the unfunded liabilities will be paid to allow for an employer contribution rate of 22 percent.

REPRESENTATIVE SEATON noted that some municipalities are paying at 10 percent, therefore, a mechanism is needed to bring them up to an equivalent unfunded liability of 22 percent by paying part of their rate for the first several years. If an employer is paying at a higher rate, he suggested that there needs to be a mechanism to divert funds for payment of PERS liability in an amount sufficient to bring that employer's contribution rate down to 22 percent.

[7:24:56 AM](#)

CHAIR HAWKER summarized that the aforementioned approach appears designed to establish parity whereby the unfunded liability for every employer is 22 percent and the consolidated employer rate is also 22 percent.

REPRESENTATIVE SEATON agreed with the aforementioned summarization and set forth it would require two different calculations to set the rate at 22 percent. He noted that the rate chosen could be different than 22 percent. He offered that his proposed amendment is not so much about the actual rate as about establishing a mechanism to bring all employers to parity with regard to their unfunded liabilities.

[7:26:43 AM](#)

REPRESENTATIVE FAIRCLOUGH noted that employers who pay into the system to "make themselves whole" sooner will have less of an obligation. She asked if that possibility had been considered when preparing the scenarios presented by the proposed conceptual amendment.

REPRESENTATIVE SEATON indicated that details of payment and interest rate accrual would still need to be considered, but reiterated that his approach requires the determination of unfunded liabilities at a particular point or "snapshot" in time. The actuarial rates for each employer are determined based on the amount of unfunded liabilities. The hold harmless provision's purpose is to work out a mechanism to bring all the employers, with their differing rates and unfunded liabilities, into a cost share system on an equitable basis.

REPRESENTATIVE FAIRCLOUGH suggested that there are many details to be worked out due to the differing situations of some employers, noting that some are over-funded, while others owe quite a bit.

[7:28:43 AM](#)

REPRESENTATIVE SEATON agreed that there will need to be adjustments made to address issues that will arise as the state moves to bring employers to an equivalent basis. He explained the calculations necessary to arrive at a consolidated rate of 22 percent. To arrive at this figure, one must calculate the difference between the past service cost rate and the normal cost rate. This difference will set the amount the employer must pay to towards its past service cost. The difference between the past service cost and the employer's rate will determine the amount of the state's contribution towards the past service cost. If a consolidated rate of 22 percent is the goal, the employers will take responsibility for 41.7 percent of the UAAL and the state share will be 58.3 percent of the UAAL. He said that the mechanisms for payment, whether through employment taxes, POBs, or other methods, will need to be determined. Using the 22 percent rate as an example would result in the employers being responsible for \$1.83 billion and state responsible for \$2.56 billion.

[7:32:49 AM](#)

CHAIR HAWKER requested an explanation of the linkage between the calculations that determine a consolidated rate of 22 percent and the actual amount of UAAL the employers and the state are responsible for.

REPRESENTATIVE SEATON explained that one must look at the past service cost rate and the normal cost rate. The difference between those sets 7.52 percent as the amount necessary to pay off the past service cost. This difference is divided by the past service cost rate to determine the employers' share of the UAAL.

CHAIR HAWKER summarized that the consolidated rate of 22 percent is being used to explain a possible mechanism for a hold harmless provision. Using 22 percent as the consolidated rate, one first determines how much that figure exceeds the normal cost rate to establish a cap amount of 7.52 percent. That cap amount is a percentage of the total past service cost rate, in this example, 41.7 percent. The 41.7 percent is applied to the overall liability to determine the proportionate amount of the liability in conjunction with the proportionate amount of the payment.

REPRESENTATIVE SEATON agreed with the above summary and reminded the committee that the 22 percent figure is for discussion purposes. He opined that the current proposed employer contribution rate of approximately 32 percent to pay off the UAAL over 25 years will not work for the system. His proposal calculates how much of the unfunded liability the employers will be responsible for if a contribution rate of 22 percent is forecast for a 25 year period. As a result, the employers will pay 41.7 percent and the state 58.3 percent of the UAAL, which must be reduced somehow, he indicated.

[7:36:54 AM](#)

CHAIR HAWKER offered his understanding that this proposal assumes a fixed employer contribution rate. He asked about the effect of future actuarial changes to the past service cost rate.

REPRESENTATIVE SEATON indicated that the current system presents a known problem of employer rates that are too high and unpredictable medical costs. This proposal suggests a way to fix the known aspects of the problem of unfunded pension liabilities.

CHAIR HAWKER sought further clarification by setting forth his understanding that the 22 percent is a fixed variable, and all other calculations are based on that rate. He indicated his understanding that the proposed mechanism would work regardless of changes to other variables, such as the past service cost rate. In that case, the amount the state is responsible for may increase or decrease annually.

REPRESENTATIVE SEATON explained that 18.03 percent is the calculation for the past service cost rate amortized over 25 years.

CHAIR HAWKER pointed out that the past service cost rate will change based on the annual actuarial valuation.

REPRESENTATIVE SEATON agreed that the past service cost rate would change but perhaps not by much unless there are large changes in the state's total liability for medical and retirement benefits. However, he reiterated his opinion that to move to a cost share system without some mechanism to lower the projected employer contribution rate of 32 percent will cause at least half of the employers to leave PERS.

[7:42:53 AM](#)

CHAIR HAWKER summarized his understanding that this approach sets a fixed amount for the consolidated rate that all PERS employers will pay. Once that fixed amount is determined, calculations are done to determine the state's share of the unfunded liabilities, while the communities are held to the consolidated rate for employer contributions.

REPRESENTATIVE SEATON suggested that POBs or other methods could be used to reduce the state's share of the UAAL.

[7:44:03 AM](#)

CHAIR HAWKER contrasted Representative Seaton's proposed hold harmless approach with that currently proposed in HB 206. He offered his understanding that the fixed element in HB 206 is the amount of the calculated UAAL as of June 30, 2006, which is "multiple billions of dollars." Under the bill, the state would pay 65 percent of the known UAAL to determine the dollar amount the state would be responsible for. The PERS employers would share the risk of future rate adjustments with the state.

ANNETTE KREITZER, Commissioner Designee, Department of Administration (DOA), clarified that the amount of the UAAL calculated as of June 30, 2006 is 8.6 billion, which she stated is a more accurate determination of the amount of unfunded liabilities.

CHAIR HAWKER explained that Representative Seaton's approach is "much more akin" to the structure currently being considered by the House Finance Committee. This debate is very relevant to section 7 of the bill, he indicated.

REPRESENTATIVE ROSES noted that when communities opt out of PERS, their termination costs are based on an actuarial calculation of that employer's share of the unfunded liabilities at the time of termination. He asked whether there is any ability for DOA to adjust the termination costs if it is later determined that the costs attributed to the employer were not accurate.

COMMISSIONER DESIGNEE KREITZER said she believes that once the opt out rate is set, DOA cannot go back and change it.

[7:51:45 AM](#)

KATHLEEN LEA, Retirement Manager, Division of Retirement and Benefits (DRB) Department of Administration explained that termination liability is determined based on a present day value calculation arrived at through an actuarial projection of an employer's future costs. She said that amount, once determined, is not adjusted.

REPRESENTATIVE ROSES offered his understanding that the finality of the termination cost decision applies regardless of whether actual liability was over- or under-assessed.

MS. LEA agreed that the aforementioned understanding is correct because the actuary uses assumptions to determine costs, so if the actual costs vary from the assumptions the amount of an employer's actual liability will adjust accordingly.

[7:53:13 AM](#)

REPRESENTATIVE GRUENBERG suggested that the law could be amended to allow some flexibility in making these determinations regarding opt-out procedures.

COMMISSIONER DESIGNEE KREITZER said she would be willing to consider any amendment, but offered that she does not see a way to structure opt-outs to allow the state to go back and adjust the determined opt-out costs. She agreed that there is an issue when opt-out costs turn out to not be accurate, but opined that it would be difficult to craft a solution to fix the problem.

REPRESENTATIVE FAIRCLOUGH offered that there could be a method to provide an opportunity for communities to come together and issue a POB to pay off their liabilities all at once. She opined that those communities who do not participate would pay interest.

REPRESENTATIVE SEATON indicated he is supportive of methods that would help communities enter a cost share system on an equal basis.

[7:58:31 AM](#)

MS. LEA reminded the committee that each employer's liability is valued annually. She pointed out that termination liability is different from an employer's unfunded liability and generally far exceeds the employer's unfunded liability. If an employer opts out, the remaining employers are valued on their own pool of employees and retirees.

REPRESENTATIVE WILSON asked if employers pay less if they stay in the PERS then if they opt out.

MS. LEA reiterated that termination costs are significantly different from an employer's unfunded liability and that it is important for communities to understand that.

COMMISSIONER DESIGNEE KREITZER opined that some communities will find it less expensive to stay in PERS then to terminate their participation.

REPRESENTATIVE ROSES suggested that one reason for establishing a consolidated rate is because there is no mechanism by which to allocate employer assets and responsibilities once those funds are transferred to the retiree reserve account. He suggested that if there is a fixed rate, any future savings or additional liabilities could be accurately allocated to the state. Under the current system, the state has shouldered responsibility for the "lion's share" of costs for the PERS and Teachers' Retirement System (TRS). If a fixed rate is established, the employers will have the ability to incorporate into their budgets an approach to reducing their unfunded liability.

[8:02:43 AM](#)

REPRESENTATIVE SEATON addressed the issue of how to determine rates for communities that have over or under paid their pension liabilities. He said that currently 63 employers pay an employer contribution rate of less than 22 percent. Under his approach, those employers whose rates would increase to 22 percent will receive a contribution from an asset pool to help them get up to the 22 percent contribution rate. This approach would help those employers arrive at the 22 percent rate over a number of years. For employers that are now paying more than 22 percent, their total employer contribution rate, minus 22 percent, is calculated to determine the "Y percent", which is then multiplied by the employer's wage base to arrive at a dollar amount. That dollar amount is transferred to PERS from the community dividend revenue sharing payment. He suggested that the amount paid out of revenue sharing be capped so that communities with a large unfunded liability will still receive some revenue sharing during the time payments are being made to bring their contribution rates down to 22 percent.

CHAIR HAWKER summarized that when the determination of the amount of the unfunded liability is made, it would result in

funds being transferred so that every employer's share of the unfunded liability would be adjusted to 22 percent.

8:07:26 AM

REPRESENTATIVE SEATON agreed that is how he proposes to assure that all employers become equivalent partners in a cost share system. He offered that there are many possible methods by which to accomplish this goal.

CHAIR HAWKER asked how this approach would benefit any employers who are currently paying below 22 percent.

REPRESENTATIVE SEATON replied that the system would pick up the difference between the employer's current rate and the 22 percent rate until the employer's actuarially unfunded liability equals 22 percent. He opined that there is a real advantage to being in PERS as it offers stability.

CHAIR HAWKER asked whether an employer's contribution rate would be calculated annually as if there was no cost sharing program.

REPRESENTATIVE SEATON explained that the calculation would be made to determine the dollar amount difference between the unfunded liability portion and each employer's share. This one-time calculation would determine the payments to be made over the years.

CHAIR HAWKER reiterated his concern that this approach does not seem to provide a benefit to any employer whose current contribution rate is below 22 percent.

8:11:57 AM

REPRESENTATIVE SEATON said that under a cost share system, all the employer contributions will be in one pool. He said that cost share pool will use off-setting contributions to pay the difference between the current contribution rate and the pool rate of 22 percent.

8:12:59 AM

REPRESENTATIVE ROSES suggested that the bill has an effect similar to Representative Seaton's suggested approach since all communities' rates would be 31.89 percent under HB 206. He clarified that his understanding of HB 206 is that an employer with a rate below 22 percent would continue to pay at its lower

rate. However, he said that under his understanding of the approach put forth by Representative Seaton, that employer would not have to make payments until such time as their rate would equal the 22 percent.

CHAIR HAWKER opined that, if correct, the aforementioned characterization would require an ongoing dual calculation of the employer's liability.

REPRESENTATIVE FAIRCLOUGH clarified that at one point in time an amortized payment schedule would determine how long an employer whose current rate is below 22 percent would not have to pay into the system. Once that amortized credit is exhausted, the employer would pay into the system at 22 percent.

REPRESENTATIVE ROSES said that some employers have over paid into the system.

REPRESENTATIVE SEATON explained that the proposed cost share plan does not take into account the differing employer histories that affect liabilities and rates. He offered that his approach presents a mechanism to allow for the fact that some employers have under paid, while others have over paid into PERS.

REPRESENTATIVE FAIRCLOUGH suggested that if a municipality currently does not pay 22 percent it will be hard to suddenly make their payments at 22 percent. She suggested that cities must remain judicious in their payments so that they are ready to assume payment at 22 percent when necessary.

[8:20:01 AM](#)

CHAIR HAWKER offered that a key difference between Representative Seaton's approach and that currently in HB 206 is creating surety for individual employers. The administration's proposal lets the employers' rates fluctuate. He indicated that there is some concern that communities will be unable to absorb large rate increases. He suggested the committee could formulate a letter of intent to express its concern that the administration's proposal does not provide the desired surety of a fixed or capped rate. If rates continue to increase, the legislature will have to continue to address the fiscal burden on communities, he opined.

[8:23:28 AM](#)

REPRESENTATIVE SEATON reminded the committee that the point is not so much to establish a set rate, but to come up with some method for employers to enter a cost share system at an equivalent point.

CHAIR HAWKER reiterated that the 22 percent rate was picked as a convenient number for discussion purposes.

REPRESENTATIVE ROSES noted that a fixed consolidated rate allows for some long range planning by employers, but does not alter their obligation to pay their unfunded liabilities.

[8:27:01 AM](#)

REPRESENTATIVE FAIRCLOUGH stated some concern with tying this approach to revenue sharing. She opined that it may be preferable to fix the system at a set point in time, and offer incentives to encourage communities to use bonds or other methods to reduce their liabilities. She reminded the committee that some communities receive very little revenue sharing funds.

CHAIR HAWKER suggested that the letter of intent should identify the main issues raised and also set forth that any approach resulting in a "winners and losers" system needs further consideration.

REPRESENTATIVE SEATON said that HB 206 has no language about how to address the issue of "winners and losers" that will occur if the state adopts a cost share approach for PERS. He suggested that a preferable approach may be to forward something more detailed to the House Finance Committee for its consideration.

[8:30:41 AM](#)

CHAIR HAWKER expressed some concern that the approach discussed today is so different from HB 206 that it is really a separate, competing piece of legislation which would require further vetting. However, he reiterated his willingness to proceed with a letter of intent that will encompass the committee's concerns with HB 206.

[8:34:21 AM](#)

CHAIR HAWKER moved to adopt a letter of intent to the House Finance Committee encapsulating the main points of today's discussions as conceptual Amendment 3.

REPRESENTATIVE SEATON objected for discussion purposes.

REPRESENTATIVE SEATON removed his objection and there being no further objection, conceptual Amendment 3 to HB 206 was adopted.

[8:38:56 AM](#)

REPRESENTATIVE SEATON moved Amendment 2, 25-GH1074\A.1, Wayne, 4/10/07, which read [original punctuation provided]:

Page 8, following line 14:

Insert a new subsection to read:

"(c) Notwithstanding AS 39.35.255, added by sec. 5 of this Act, an employer that made employer contributions under former AS 39.35.270 for the period beginning July 1, 2002, and ending June 30, 2006, that, when combined, exceed the minimum required of the employer for that period by former AS 39.35.270 shall receive a credit equal to the excess and may apply the credit toward payment of employer contributions under AS 39.35.255 for subsequent years."

REPRESENTATIVE FAIRCLOUGH objected.

[8:39:55 AM](#)

REPRESENTATIVE SEATON explained that Amendment 2 allows employers to receive a credit for excess contributions. He said that if the House Finance Committee adopts some kind of mechanism to account for overpayments, Amendment 2 would not be needed. However, if no mechanism to account for overpayments is adopted, then Amendment 2 provides a mechanism to determine a credit amount for those employers who have made extra efforts to pay their unfunded pension liabilities. The time period chosen is the time for which the unfunded liability was determined. He noted that 22 communities made extra payments towards their unfunded liabilities.

REPRESENTATIVE FAIRCLOUGH suggested that Amendment 2 should be inserted in a different section of the bill than stated in the amendment.

[8:43:48 AM](#)

REPRESENTATIVE SEATON withdrew Amendment 2 and offered conceptual Amendment 2 which would have the same wording as Amendment 2, but would be inserted in the most appropriate place in HB 206.

CHAIR HAWKER objected for discussion purposes. There being no further objections or discussion, Chair Hawker withdrew his objection to conceptual Amendment 2 and it was adopted by the committee.

[8:45:22 AM](#)

REPRESENTATIVE GRUENBERG offered Amendment 1, 25-GH1074\A.4, Wayne, 4/09/07, which read [original punctuation provided]:

Page 7, following line 31:

Insert a new bill section to read:

"* **Sec. 15.** AS 39.35.260(b), enacted in sec. 7 of this Act, is repealed July 1, 2008."

Renumber the following bill sections accordingly.

Page 8, line 28:

Delete "Sections 15 and 16"

Insert "Sections 16 and 17"

Page 8, line 29:

Delete "sec. 18"

Insert "sec. 19"

CHAIR HAWKER objected for discussion purposes.

[8:45:38 AM](#)

REPRESENTATIVE GRUENBERG opined that there are many variables to consider when determining the merits of a cost share system. He stated his opinion that the legislature should be able to revisit these issues, and that Amendment 1 would provide that opportunity.

CHAIR HAWKER said he has some concerns regarding Amendment 1.

[8:48:01 AM](#)

COMMISSIONER DESIGNEE KREITZER opined that the provisions in Amendment 1 may force DOA to renegotiate at a time that may not be appropriate. She suggested that the legislature has the

ability to re-visit issues at any time, and that a one-year sunset provision would actually be more constraining by setting a specific time to re-visit the issues covered by the bill.

REPRESENTATIVE GRUENBERG set forth that he is not committed to the approach in Amendment 1, but suggested there may be some need to follow up on how the cost share provisions are working.

COMMISSIONER DESIGNEE KREITZER suggested that legislative committees with jurisdiction over DOA could request that the Commissioner appear to present information on the progress of the PERS\TRS issues.

REPRESENTATIVE FAIRCLOUGH stated she opposes Amendment 1 as it will sunset section 7 of HB 206 possibly before debate on the issue is closed.

REPRESENTATIVE GRUENBERG withdrew Amendment 1.

CHAIR HAWKER reminded the committee that the PERS liability is one of the paramount issues facing the state and it will likely remain in public view.

[8:54:02 AM](#)

REPRESENTATIVE FAIRCLOUGH moved to report HB 206, Version 25-GH1074\A, as amended, out of committee with individual recommendations and the accompanying indeterminate fiscal notes. There being no objection, CSHB 206 (W&M) was reported from the House Special Committee on Ways and Means.

[Patrick Shier, Director, Division of Retirement and Benefits, was introduced to the committee.]

ADJOURNMENT

There being no further business before the committee, the House Special Committee on Ways and Means meeting was adjourned at [9:03:26 AM](#).