

**MINUTES**  
**SENATE FINANCE COMMITTEE**  
**March 14, 2007**  
**9:35 a.m.**

**CALL TO ORDER**

Co-Chair Bert Stedman convened the meeting at approximately [9:35:43 AM](#).

**PRESENT**

Senator Lyman Hoffman, Co-Chair  
Senator Bert Stedman, Co-Chair  
Senator Kim Elton  
Senator Donny Olson  
Senator Joe Thomas  
Senator Fred Dyson  
Senator Charlie Huggins

**Also Attending:** SENATOR STEVENS; REPRESENTATIVE HAWKER; ANNETTE KREITZER, Commissioner, Department of Administration; CHARLENE MORRISON, Chief Financial Officer, Division of Retirement and Benefits, Department of Administration.

**Attending via Teleconference:** There were no teleconference participants.

**SUMMARY INFORMATION**

^PERS Defined Benefit Plan Accounting  
Presentation by Division of Retirement and Benefits

[9:35:53 AM](#)

ANNETTE KREITZER, Commissioner, Department of Administration, gave an introduction to presentations on the policy goals of two bills that would be introduced by Governor Sarah Palin's Administration in the coming weeks. The first bill related to "technical fixes" within the Public Employees Retirement System (PERS), pertaining to death and disability benefits. The second bill was referred to as a "cost share bill," necessitated by accounting issues within PERS. This presentation would address the accounting concerns.

Ms. Kreitzer informed that presentations would be on-going to "show the Committee each step of a plan that starts with shifting to cost share plan; how doing that impacts the State and local governments' bottom line; how we can keep costs down for all of us and address the unfunded liability." She noted that \$355 million was currently included in the FY08 budget to fund State employees' pension costs, and that figure did not include pension costs for the University, the legislature, the Alaska Court System or the Alaska Marine Highway System.

[9:39:07 AM](#)

CHARLENE MORRISON, Chief Financial Officer, Division of Retirement and Benefits, Department of Administration, began her presentation which was accompanied by a handout titled, "Public Employees' Retirement System (PERS), Defined Benefit (DB) Plan, Accounting Issues, Senate Finance, March 14, 2007" [copy on file].

AT EASE [9:39:39 AM](#)/[9:41:07 AM](#)

[9:41:13 AM](#)

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Why are we here today?

- ❖ Concerns about employer level accounting for the PERS DB plan.
- ❖ Contribution rates for PERS DB plan not supported by employer level accounting records.
- ❖ Set the stage to discuss the proposed solution.

Ms. Morrison reviewed the page.

[9:41:43 AM](#)

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Proposed Solution

Cost share legislation

- ❖ Administer the PERS DB plan like the TRS DB plan

- ❖ State to assume 65% of unfunded liability at 6/30/2006 (estimated \$3.6B of \$5.5B total)
- ❖ All employers share the cost (benefits, administration and investment)
- ❖ Simplify administration

Ms. Morrison overviewed the page, adding that the unfunded liability is not yet known for June 30, 2006.

[9:42:45 AM](#)

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Proposed Solution (cont.)

Address the unfunded liability

- ❖ If market conditions warrant, use pension obligation bonds as part of solution to reduce the unfunded liability.

Ms. Morrison summarized the page.

[9:43:03 AM](#)

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PERS = One System but Two Plans

- ❖ Defined Benefit Plan (Tiers I, II, and III)
- ❖ Defined Contribution Retirement Plan (Tier IV)

Ms. Morrison read the page, referring to the Defined Contribution Retirement Plan as the "hybrid plan".

[9:43:44 AM](#)

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PERS DB Accounting Issues

No impact on:

- ❖ Teachers' Retirement System (TRS)
- ❖ Benefits paid to members
- ❖ PERS DB Plan level accounting (PERS as a whole)

- ❖ New PERS Defined Contribution Retirement Plan (Tier IV)

Ms. Morrison reviewed the page. She noted that many "pieces" of the PERS Defined Benefit (DB) issues had been studied throughout the State, but she would focus on two primary issues.

[9:44:29 AM](#)

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Agent Multiple Employer Plan

Defined and described as follows:

- A plan that provides benefits to employees of more than one employer
- ❖ Pooled administrative and investment functions
  - ❖ Share costs/income of pooled functions
  - ❖ Separate accounts for each employer
  - ❖ Each employer's contributions are to provide benefits only for that employer's employees

Ms. Morrison overviewed the information.

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Alaska Statutes

AS 39.35.100(b)(3)

- ❖ A separate account for each employer shall be maintained.
- ❖ The account shall be credited with contributions of the employer.
- ❖ This account shall be charged with the employer's actuarial charge for pension, death benefits, and other benefits paid under this plan to or on behalf of the employee of the employer.

Ms. Morrison reviewed the page, adding that although the Alaska statutes do not use the term "multiple employer plan," they require many of the same components.

[9:45:51 AM](#)

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Alaska Statutes (cont'd)

- ❖ AS 39.35.680 (22) defines employee as "...a retired member..."
- ❖ AS 39.35.250 states that the past service portion of the employer's contribution rate is that "required to amortize the unfunded obligations of the employer..."

Ms. Morrison read the page.

[9:46:12 AM](#)

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PERS DB Plan

[Flow chart showing the following:

Assets

- Investment Income
- Contributions
  - DB Employee
  - DB Participating Employer

Minus

Liabilities

- Pension Benefits
- Health Costs
- (both measured annually)

Equals

Surplus or (Unfunded Liability)  
Employer responsible for funding shortfall]

- ❖ This calculation is performed at the employer level as well as at the plan level
- ❖ There are concerns regarding employer level accounting and allocation methodologies in use

Ms. Morrison walked the Committee through the chart.

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## Assets

Employer contributions are accounted for in two separate buckets:

- ❖ Active employer asset accounts
  - o One account for each individual employer
- ❖ Retiree reserve asset account
  - o One consolidated account for all participating employers

Ms. Morrison overviewed the page, commenting that there were 160 individual employers participating in the PERS DB plan, the largest of which is the State of Alaska. The retiree reserve account has caused concerns due to the fact that it is a "consolidated" account, and therefore accounting is not maintained at the employer level.

[9:47:48 AM](#)

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## Retiree Reserve Account

### Funding Sources

- ❖ Share of the plan's net investment income
- ❖ Transfers from the active employer's asset accounts

Ms. Morrison read the page, noting that the lack of employer maintenance was an issue to be discussed in this presentation.

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## Transfers

- ❖ In order to calculate an employer's past service contribution rate, we assign retiree reserve assets to employers

- ❖ Allocation process is used to assign retiree reserve assets to individual employers

Ms. Morrison summarized the page.

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#### Allocation Process

Allocate retiree reserve account balance to employers resulting in employer's retiree reserve account balance

- ❖ based on the employer's pro rata share of retiree liabilities at year end
- ❖ The amount allocated to an employer does not represent contributions made by the employer
  - o simply represents assets assigned
- ❖ Concerns have been raised about this practice - no accounting by individual employer.

Ms. Morrison reviewed the information on the page.

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#### Allocation example

Participating employer has the following assets and liabilities in the Plan at 6/30/04.

[Table depicting the following:

##### Assets

Active: \$237,819

Allocated share of retiree reserve account: -

Total: \$237,819

##### Liabilities

Active: 350,172

Allocated share of retiree reserve account: -

Total: 350,172]

- ❖ Unfunded liability is \$112,353

- ❖ Employer has no retirees at 6/30/2004, so has not contributed to the retiree reserve account

Ms. Morrison overviewed the example provided.

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Next year - FY05

Employer now has retirees in the plan for the first time so will get an allocation of the retiree reserve account balance based on their retiree liabilities compared to total retiree liabilities even though they have not contributed to the retiree reserve account in the past.

Ms. Morrison continued with the example overview.

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The allocation  
[Table depicting the following:

Employer retiree liabilities:	\$453,428
Total retiree liabilities	7,131,974,579
% allocated to employer	.006%
Retiree reserve account balance	6,194,055,956
Account balance allocated to employer	\$393,883
Even though employer has not contributed to this account]	

Note: This is the impact if the employer's retiree liabilities are growing; however, the reverse is the impact if the employer's retiree liability is declining.

Ms. Morrison summarized the page, stressing that the employer would receive a deduction to their retiree reserve balance if their retiree liabilities decreased rather than increased.

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Transfer

AS 39.35.100 states, "Upon retirement, the amount actuarially determined...to fully fund benefits...shall be transferred...from the employer contribution account into the retirement reserve account."

- ❖ Transfer, from the employer's active asset account, the balance needed to fully fund the employer's retiree reserve asset account
  - o Compare the assigned assets to the allocated liabilities and transfer the difference

Ms. Morrison reviewed the page.

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The transfer

Per statute, the retiree reserve account is to be fully funded.

[Table depicting the following:

Employer retiree liabilities	\$453,428
Account balance allocated to employer	393,883
Amount transferred from employer active account	\$59,545]

Ms. Morrison read the information on the page, adding that the employer would be responsible for contributing the balance necessary after the transfer to fully fund its retirement obligations, as required by statute.

[9:53:10 AM](#)

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Effect of allocation and transfer

Participating employer has the following assets in the Plan at 6/30/05 after transfer to fully fund the retiree reserve account.

[Table depicting the following:

Assets:

Active

(237,819 + 32,261 - 59,545)

\$210,535

Allocated share of retiree reserve account

(393,883 + 59,545)

453,428

Total

\$663,963

Liabilities:

Active

(237,819 + 32,261 - 59,545)

\$18,107

Allocated share of retiree reserve account

(393,883 + 59,545)

453,428

Total

\$471,535]

❖ Over funded by \$192,428.

Ms. Morrison summarized the exemplified calculation, commenting that, as previously mentioned, the employer could find their retirement obligations underfunded if their retirement liabilities were declining instead of increasing.

[9:54:06 AM](#)

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Liabilities

Annually calculated by employee

❖ Allocated to individual employer

o Based on pro rata service earned with employer

o Does not take into account salary earned with employer

- o Concerns have been raised about this allocation process as well

Ms. Morrison informed that an individual's liabilities are allocated to each employer if the employee had more than one participating employer.

[9:54:38 AM](#)

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#### Liability allocation example

One employee is a covered elected official for the City of X for 5 years earning 5 years of service credit. Is paid \$1,000 for attending meeting during these 5 years.

Same employee worked for City of Z for 5 years prior to serving as elected official. Was paid \$200,000 for the 5 year period.

Ms. Morrison read through the example.

[9:55:08 AM](#)

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#### Example (cont.)

Actuary calculates a \$750,000 liability for the member. This liability is allocated to employers as follows:

[Table depicting the following:

City of X	
Salary Paid:	\$1,000
Service Earned:	5 yrs
% by employee	50%
Liability allocated	\$375,000
City of Z	
Salary Paid:	\$200,000
Service Earned:	5 yrs
% by employee	50%
Liability allocated	375,000

Total	
Service Earned:	10 yrs
% by employee	100%
Liability allocated	\$750,000]

Note: Extreme example to clearly reflect the impact of the current practice. Approximately 735 or 1.2% of all PERS members have service in both categories shown above.

Ms. Morrison reviewed the example, noting that this calculation was the current practice.

[9:56:04 AM](#)

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Impact on Contribution Rates

Assets - Liabilities = Surplus or (Unfunded Liability)

Concerns raised about both the assets and liabilities assigned to employers, individually, and collectively, impact the employer's unfunded liability.

Unfunded liability - basis of the past service cost portion of the employer's contribution rate.

Ms. Morrison summarized the page.

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Proposed Solution

Cost Share Legislation - long range

- ❖ Redesign the PERS DB plan - align with TRS
  - o All employers share the cost/income of the Plan (benefits, administration, and investment)
  - o One uniform, less volatile, contribution rate
- ❖ ARMB supports concept - Resolution 2007-04
- ❖ AML supports concept
- ❖ Administration of plan simplified
- ❖ Will be introduced by the Governor

Ms. Morrison reviewed the information.

[9:57:38 AM](#)

Senator Thomas asked if the example on page 23 was the current or proposed practice.

Ms. Morrison answered that it was an example of the current practice.

Senator Thomas asked how the proposed solution would change that calculation.

Ms. Morrison responded that all employers would share equally in the cost of the plan, and would no longer maintain individual employer information.

[9:58:38 AM](#)

Senator Thomas furthered, asking if annual statements were sent to employees.

Ms. Morrison affirmed, clarifying that employees enrolled in the defined benefit plan receive annual statements, and those enrolled in the defined contribution plan receive statements quarterly.

[9:59:04 AM](#)

Senator Elton, referring to the statutory requirements listed on pages 8 and 9 and "concerns raised" over employer contributions, asked if ambiguity exists regarding liability accruals

[9:59:58 AM](#)

Ms. Morrison replied that the liabilities are known, as that figure is calculated by the member. The "concerns" regard the assets, as the State currently operates under a consolidated retiree reserve assets account that does not account for each employer's contributions.

[10:00:16 AM](#)

Senator Elton asked if the current practice violates the statutory requirements.

[10:00:29 AM](#)

Ms. Kreitzer answered: "I don't know that we've been in contravention with the statute. I would say that this has been the practice of the State for the last twenty years. I'm now the Commissioner Designee for the Department of Administration; I'm here to help you."

[10:00:54 AM](#)

Senator Elton continued, speaking to the proposed solution of a "65/35" cost share of retirement obligations between the State and municipalities. He was aware of other proposed cost share ratios, and asked how flexible the Administration would be to amending that figure.

Ms. Kreitzer suggested the Department present the entire plan to the Committee before discussing the cost share ratio.

[10:02:14 AM](#)

Co-Chair Hoffman asked the proposed implementation date of the legislation.

Ms. Kreitzer set the effective date as July 1, 2007.

Co-Chair Hoffman asked how the calculations would address the long-term unfunded liability.

Ms. Kreitzer was not prepared to answer the question, and anticipated that discussion beginning with the introduction of the cost share legislation. She would present the Committee with a "long-term vision" that could include a General Fund "infusion" into the retirement system, and possibly pension obligation bonds. The Administration anticipated addressing 80 percent of the unfunded liability.

Co-Chair Hoffman asked if participation bonds would be introduced as separate legislation.

[10:03:41 AM](#)

Ms. Kreitzer informed that House Bill 13 had been introduced and that bill spoke to the bonding issue. It would allow pension

obligation bonds if passed by the legislature. The Department would present additional information regarding the bond option at a later date.

[10:04:34 AM](#)

Senator Huggins asked if the municipalities supported the legislation.

Ms. Kreitzer had heard presentations from the Alaska Municipal League (AML), and had spoken to a few members. The Department had taken public comments into consideration while drafting the legislation, and would meet formally with AML.

Senator Huggins asked the reaction of AML thus far in the process.

[10:05:17 AM](#)

Ms. Kreitzer responded that AML members had not yet taken a position, as the Administration had not had the opportunity to present the complete plan.

[10:05:40 AM](#)

Co-Chair Stedman identified three issues the Committee would address in the coming months. The first was a "clean-up" bill to Senate Bill 141, retirement system legislation passed by the 24th Legislature. The second issue would be the cost share bill, and the third issue would be addressing the unfunded liability. He anticipated the "clean-up" bill and the cost share bill would be before the Committee in the coming weeks.

[10:06:54 AM](#)

Senator Thomas asked the Department's position on the use of obligation bonds.

[10:07:17 AM](#)

Ms. Kreitzer replied that the Department would present the effects of using pension obligation bonds to address a portion of the unfunded liability, focusing on the long-term savings that would provide.

Senator Thomas queried if that discussion would include tax exempt bonds.

Ms. Kreitzer responded that the Department had concentrated on pension obligation bonds. She looked forward to the cost share bill serving as a "vehicle" to examine possible solutions for the unfunded liability facing the State.

#

**ADJOURNMENT**

Co-Chair Bert Stedman adjourned the meeting at [10:08:46 AM](#)