

MINUTES
SENATE FINANCE COMMITTEE
March 19, 2007
9:06 a.m.

CALL TO ORDER

Co-Chair Bert Stedman convened the meeting at approximately [9:06:02 AM](#).

PRESENT

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

Also Attending: ANNETTE KREITZER, Commissioner, Department of Administration; MELANIE MILLHORN, Director, Division of Retirement and Benefits, Department of Administration;

Attending via Teleconference: There were no teleconference participants.

SUMMARY INFORMATION

SB 125-PERS CONTRIBUTIONS; UNFUNDED LIABILITY

The Committee heard from the Department of Administration. The bill was held in Committee.

#SB125
[9:07:21 AM](#)

SENATE BILL NO. 125

"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."

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

Co-Chair Stedman reminded of accounting issues of the Public Employees Retirement System (PERS) and the Teachers Retirement System (TRS) discussed the previous week and of "challenges" to these systems that were learned. This bill, in addition to SB 123 relating to technical corrections to the Tier IV plan, would address those challenges.

[9:09:35 AM](#)

ANNETTE KREITZER, Commissioner, Department of Administration, introduced Ms. Millhorn.

[9:09:51 AM](#)

MELANIE MILLHORN, Director, Division of Retirement and Benefits, Department of Administration, gave an opening statement as follows.

This presentation will be comprised of two parts: (1) overview of SB 125 PERS Cost Share Bill and (2) financial proposal to address unfunded liability for PERS and TRS, which will be presented by Commissioner Kreitzer.

On March 13, 2007, you received a presentation from Charlene Morrison, Chief Financial Officer and Commissioner Kreitzer.

During the presentation it was explained that PERS Plan is an agent multiple employer plan, which means that the assets are pooled for all PERS employers and they share the administrative expenses.

Currently, in accordance with statute, each PERS employer has its own individual employer contribution rate that it pays to the PERS Plan. The employer contribution rates vary from between 14.48% to 185% of covered payroll. There are 160 employers that participate in the PERS Plan, the State being the largest employer.

The presentation on March 13, 2007, formed the backdrop for our discussion this morning. The information provided to you involved the concerns raised about the accounting associated with the PERS Plan at the employer level. It is important to note, this matter does not impact the economics at the plan level.

Governor Palin has introduced SB 125 as a proposed solution to address the concerns raised by moving forward and establishing the PERS Plan as a COST SHARE PLAN.

SB 125 is molded after the TRS Plan, which is a cost share plan established by the legislature in 1955. All TRS employers pay one uniform rate. There are 58 employers that participate in the TRS plan.

Under SB 125 there will be no assignment of liabilities and assets by individual employer. Instead all employers will share in the liabilities and the assets - hence the name "Cost Share Plan".

This bill will establish one uniform employer contribution rate for PERS employers, with the exception that the State of Alaska will pay a higher contribution rate.

[9:12:18 AM](#)

Ms. Millhorn gave a PowerPoint presentation titled, "Senate Bill 125 Overview, PERS Cost - Share Bill" [copy on file].

[9:12:37 AM](#)

Page 2

Purpose of Cost-Share Bill

- Assigns the state 65% of the unfunded liability at 6/30/2006 (estimated \$3.6 billion of \$5.5 billion total)
- Employers would pay uniform rate (31.86%-FY 08), except state would pay higher rate (47.92%-FY 08)
- All employers share cost (benefits, administration and investment)
- Simplifies administration of plan

Ms. Millhorn read this information into the record. The Cost-Share method would simplify administration of the retirement program because it would eliminate the need to account for assets and liabilities at the employer level.

[9:13:34 AM](#)

Page 3

Section 1 - AS 39.35.100

- Repeals prior language on separate employer accounts
- Eliminates Retiree Reserve Account
- States how pension benefits will be paid
 - o Employee account exhausted first
 - o Plan funds benefits after employee account exhausted

Ms. Millhorn stated that this legislation would create "one integrated system" of accounting for all employers. Existing statutory language provides for separate accounts for each employer. Issues surrounding the Retiree Reserve Account would be eliminated, as it would be no longer necessary.

Ms. Millhorn explained that pension benefits would first be paid from the employee contribution account. When the employee account is exhausted, the plan would fund future benefits. The new system would provide that the plan "as a whole" would be responsible for funding benefits after an employee's account is depleted. This "aligns" with a cost share plan design.

[9:14:38 AM](#)

Page 4

Section 2 - AS 39.35.115

- Adds two subsections
 - o (d) joint contributory plan
 - o (e) allocates excess assets at plan termination

Reason

- Clarifies who contributes
- Section (e) required by IRS

Ms. Millhorn noted that the TRS Plan also employs a joint contribution methodology. This bill would clarify that both employees and employers submit mandatory contributions to the PERS Plan. This bill would also provide that upon termination of

the plan, if all liabilities of the plan have been satisfied, any excess assets revert to the employers as determined by the administrator, subject to approval by the federal Internal Revenue Service (IRS). Termination occurs when a member employer opts to discontinue participation in the plan.

[9:15:23 AM](#)

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Establishes Cost-Share Plan

Section 5 - AS 39.35.255

- Defines required employer contribution rate
- Defines how rate is applied
- Specifies minimum contribution rate
- Sets timing for contribution payment
- Defines contribution level for rehired retirees
- Defines normal cost and past service rates

Section 19

- Cost-share effective date July 1, 2007

Ms. Millhorn explained that employers would be required to contribute to the plan an amount representing the employer rate as approved by the Alaska Retirement Management Board (ARM). The employer rate is calculated as the normal cost rate plus the past service rate. The rate would be applied to the total of "all PERS salaries" for the employees that participate in the system. The employer rate could be no less than the normal cost rate, a requirement established with the passage of SB 141 relating to changes to the retirement system by the 24th Legislature. Contributions must be remitted within 15 days of the close of the employer's pay period, under the provisions of this bill. Past service contributions for retirees rehired under the Retiree Return Program would be paid at the same level that the employer is paying for active employees. Language in current statute for past service rate is based on an individual employer; new language for past service rate would align with cost share plan design, which would be "uniformly determined for all employers and applicable to each employer."

[9:16:50 AM](#)

Page 6

Section 6 - AS 39.35.260

- Requires rate to be calculated annually

- Requires participating employers to budget for contributions

Ms. Millhorn informed that this would change the annual calculation of the employer rate from a separate employer rate to one uniform employer rate.

[9:17:19 AM](#)

Page 7

Section 7 - AS 39.35.260

- Adds subsection (b)
 - o Assigns 65% of unfunded liability to state at 6/30/2006
 - o Remaining 35% of unfunded liability to other PERS employers
 - o Stipulates rate conditions

Ms. Millhorn outlined this information. The State's portion of the unfunded liability of \$5.5 billion would be \$3.6 billion and the remaining employers' portion would be \$1.9 billion.

Ms. Millhorn remarked, "Once the rate for the State of Alaska, as calculated in this subsection, is within one percentage point of the rate for all other PERS employers, a separate rate for the State" would no longer be calculated.

[9:18:19 AM](#)

Page 8

Section 9 - AS 39.35.610(b)

- o Provides for intercept in event employer does not make timely contributions

Ms. Millhorn pointed out this language would add a new section to statute. It would allow the administrator of the PERS Plan to "intercept the amount of contributions and interest due from an employer" in the event that an employer fails to make timely payment contributions. It would also allow the administrator to claim delinquent contributions and interest "from any agency of the State or political subdivision that has funds in its possession of the employer that are to be distributed to the employer that are not restricted by statute or appropriation to a specific purpose." This would provide a method for collection of overdue contributions and to prevent one employer "in

default" from adversely affecting the rate "shared by all employers in the plan."

[9:18:56 AM](#)

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Section 10 - AS 39.35.615

- o Addresses voluntary termination provisions and allows employer to terminate from plan
- o Prevents amendments to participation agreement under cost-share design

Ms. Millhorn stated that two sections of the bill address termination. Section 10 would allow an employer to voluntarily terminate from the plan. It would also "remove the ability" of an employer to amend its participation agreement. Under the current plan, an individual employer funds any related costs as a result of amendments to its participation agreement. However, with a cost share plan, amendments by one employer have the potential to create liability to all of the employers participating in the plan.

[9:20:09 AM](#)

Page 10

Section 11 - AS 39.35.615(g)

- o Sets timeframe for termination cost payment
 - o Payment plan or lump sum
- o Allows for intercept of funds
- o Provides for refund of excess assets, if any
- o Allows for employer to join DCR [Defined Contribution] Plan if termination cost paid in full

Section 11 - AS 39.35.615(h)

- o Requires employer pay termination costs

Ms. Millhorn explained that these provisions would require an employer terminating from the plan to pay the termination costs within 60 days of their assessment. This could be paid in increments or in full, and funds allocated to the employer from other State agencies could be "intercepted" as payment for delinquent termination costs. Refund of excess assets would be made to the employer if those assets exceed the termination costs and if in compliance with IRS regulations. An employer could rejoin the plan at a future date once termination costs were paid in full.

[9:20:25 AM](#)

Page 11

Section 12 - AS 39.35.620(i)

- o Sets timeframe for involuntary termination cost payment
 - o Payment plan or Lump sum
- o Allows for intercept of funds
- o Provides for refund of excess assets, if any
- o Allows for employer to join DCR Plan if paid in full

Section 12 - AS 39.35.620(j)

- o Requires employers under involuntary termination to pay termination costs

Ms. Millhorn announced that this pertains to an employer's involuntary termination from the plan and because she described the provisions of Sections 10 and 11, she would not repeat the same information.

[9:21:32 AM](#)

Page 12

Section 13 - AS 39.35.650

- o Clarifies employer refund conditions
 - o Plan's termination
 - o Employer's termination, if assets exceed liabilities

Reason

- o Clarification of statute
 - o Codify existing practice
- o Comply with IRS Code

Ms. Millhorn noted the refund could only be made if the assets exceed liabilities at the time of termination.

[9:22:26 AM](#)

Page 13

Section 15

- o Transition
 - o Provides for notification to employer of employee groups covered under participation agreement
 - 90-day time limit for amendments
 - o Past service credit not allowed during transition

Section 18

- o Immediate effective date for employer notification

Ms. Millhorn explained that Section 15 would provide for the administrator to notify every employer in the defined benefit plan of the departments, groups, or other classifications of employees the employer currently covered under their participation agreement. Employers would have 90 days from receipt of the notification to request an amendment to their participation to either add or delete covered groups. Once the 90 days elapsed, employers would no longer be allowed to amend their agreement in this manner.

[9:23:56 AM](#)

Page 14

Section 16

- o Transition
 - o Provides for adoption of regulations

Section 18

- o Immediate effective date to promulgate

Section 17

- o Reviser's Instructions
 - o Change headings
 - AS 39.35.615 (voluntary termination)
 - AS 39.35.620 (involuntary termination)

Ms. Millhorn outlined these provisions.

[9:24:33 AM](#)

Page 15

Cost-Share Legislation

- o Redesign PERS, DB plan - align with TRS
 - o All employers share cost/income of plan (benefits, administration, investment)
 - o Uniform, less volatile, contribution rate
 - o Resolves accounting issues
- o ARMB supports concept - Resolution 2007-04
- o AML [Alaska Municipal League] supports concept
- o Plan administration simplified
- o Introduced by Governor as proposed solution

Ms. Millhorn read this information to "summarize and recap" the presentation.

9:25:38 AM

Commissioner Kreitzer testified from her written notes as follows.

For the last two years and coming into this year, rate relief for PERS/TRS employers has been a focus of the Legislature. With the introduction of SB 125, we hope to broaden the discussion to include other options.

At a minimum, the cost-share bill does the things Ms. Millhorn outlined for you in her presentation:

It resolves the issue of separate accounting for employer contributions; It will address the issue that was raised about members who work for more than one employer and have liabilities assigned to the different employers based on service and not on salary - employers do not believe this is equitable. This will no longer be a concern by implementing a cost-share plan.

There are some pieces of this bill that could be contentious.

- The bill as written, requires municipalities to choose employees to be covered in the plan. They have 90 days from the effective date of this bill to do that. It removes some of the flexibility they now enjoy. But, like TRS, a PERS cost-share plan means that costs are shared among employers and we've tried to level the playing field for all municipalities.
- Unlike the Alaska Municipal League plan - which advocated the State pick up 85% of the unfunded liability; or HB179, which advocates an 80/20 split and a 5% employee contribution; SB 125 is Governor Palin's discussion document for looking at the whole picture of PERS/TRS funding. Moving to a PERS cost-share plan allows all employers to pay one rate, which encompasses 35% of the \$5.5 billion unfunded liability. That will bring rates down, and it will save local governments money in their FY08 budgets.
- If a local government abdicates its responsibility to pay its costs, SB 125 allows the State to intercept any State funds bound for that community. This may

sound drastic, but as the ultimate deep pocket, the State should have the flexibility to use this tool if it fits the situation.

- Making a local government pay for a termination study will save the plan from folks who just want us to run numbers. Every time we do that, everyone else in the plan pays for it. We raise it here as a policy issue.

That's all that's in the bill, but as I said the last time I was here before you, we've tried to look at the situation holistically. Instead of rate relief every year, can we take a longer range view, still impact the State and local governments' FY08 budgets in a positive way, and pay down the unfunded liability so it doesn't continue to grow?

You'll have the technical fix bill before you tomorrow, which allows us to calculate the employer rate across the entire wage base. That change won't have much impact for several years, until there are more employees in the defined contribution plan - but, it will help keep the rate lower. Employers will contribute the same; the rate will simply appear lower.

So let's talk about what happens if the State:

- o adopts this cost-share plan,
- o is allocated 65% of the unfunded liability,
- o holds harmless employers who would in FY08 have to pay more,
- o and if the State were to pay down 30% of the unfunded liability through pension obligation bonds

In addition:

- o the State puts \$500.0 million toward extinguishing the TRS liability and takes the risk for \$2.0 billion in pension obligation bonds.

[9:30:02 AM](#)

Commissioner Kreitzer overviewed "Cost Share Exhibits" [copy on file.] She intended to demonstrate to the Committee the "thought process" in developing this legislation. As concerns and issues were raised, the Committee could understand how the proposed plan was reached.

Exhibit 1

Estimated PERS Contributions

Level \$ Amortization - Change to Cost Share-
Before 65/35 and POBs

Winners and Losers - FY 08 Base

[Five page spreadsheet listing every participating employer and corresponding figures for Gross Salaries Estimated FY 08 (FY 07 gross salaries plus 3%); FY 08 Board Requested Rate; FY 08 Estimated Contribution-Original; Average Rate - 05 valuation with level \$ amortization; FY 08 Estimated Contribution - Straight Cost Share; Loser FY 08 cost share > FY 08 original; and Winner FY 08 cost share < FY 08 original.]

Commissioner Kreitzer reported that if the PERS plan converted to a "pure" cost share plan in which the State and all employers paid the same percentage in contributions, the State would "save" \$36 million, \$25 million of which would be general funds. However, such savings would cost all other employers approximately \$52 million. She did not anticipate this would receive popular support. The contribution rate for all employers, including the State, would be 39.76 percent.

[9:31:02 AM](#)

Exhibit 2a

Estimated PERS Contributions

Level \$ Amortization- Cost Share 65% SOA- \$1.7B in POB
Winners FY 08 Base

[Two page spreadsheet listing those employers whose contribution rates would decrease from the FY 08 ARM Board Requested Rate. Information for each includes Gross Salaries Estimated FY 08 (FY 07 gross salaries plus 3%); FY 08 Estimated Contribution; Average Rate (FY 05 valuation); Cost Share Contributions in FY 08; and Winners - FY 08 cost share < original FY 08.]

Commissioner Kreitzer stated that this spreadsheet shows "who the winners would be" under the proposed cost-share plan in which the State accepts 65 percent of the liability. The contribution rate requested by the ARM Board for these employers would be higher than the Average Rate of 31.86 percent proposed for FY 08 in the cost share legislation.

[9:31:36 AM](#)

Exhibit 2b

Estimated PERS Contributions

Level \$ Amortization- Cost Share 65% SOA- \$1.7B in POB
Losers FY 08 Base

[Three page spreadsheet listing those employers whose contribution rates would increase. Information for each includes Gross Salaries Estimated FY 08 (FY 07 gross salaries plus 3%); FY 08 Estimated Contribution; Average Rate (FY 05 valuation); Cost Share Contributions in FY 08; and Losers - FY 08 cost share > original FY 08.]

Commissioner Kreitzer explained this spreadsheet shows those employers with ARM Board requested rates for FY 08 that are lower than the proposed Average Rate. The rate for the State of Alaska would increase from 44.01 percent to 47.92 percent under the provision in which the State would accept 65 percent of the liability.

[9:31:54 AM](#)

Exhibit 3

Estimated PERS Contributions

Level \$ Amortization-Cost Share-65% SOA-\$1.7B in POB
Winners/Losers FY 07 as Base
Hold Harmless

Listing includes political subdivisions and school districts that have received rate relief in the past.

[Four page spreadsheet listing employers whose contribution rates would increase from their FY 07 rate and the corresponding figures for Gross Salaries, Estimated FY 07 (FY 06 plus 3%); Gross Salaries, Estimated FY 08 (FY 07 plus 3%); FY 07 Adjusted Contribution Rate; FY 08 Board Requested Rate; Average Rate (FY 05 valuation); Cost Share Contributions in FY 08; Losers FY 08 cost share > FY 07; Winners FY 08 cost share < FY 07. The State of Alaska is not included in this list, nor are several other employers.]

Commissioner Kreitzer directed attention to the total amount listed in the Losers column of \$82 million, which is the increase from FY 07 to FY 08 for all employers. This amount would be necessary to hold harmless the employers.

[9:32:29 AM](#)

Exhibit 4

[Spreadsheet containing the following information with dollars listed in millions:

PERS

Contributions estimated in FY 07 (all sources)	\$354.8
FY 08 Legislation and operating budget	
SB 52/HB 97 Education Bill	
Rate relief for school districts	
PERS/TRS contributions	\$ 37.0 GF
SB 50/HB 95 Budget Bill	
PERS Municipal and Political Sub Division	
Rate relief	\$ 77.5 GF
Governor's Budget Amendments	
PERS Payroll Base Correction (line 25)	\$ 0.6 GF
PERS Non-School Dist. ER rate increase	
Relief (line 26)	\$ 0.2 GF
PERS School Dist. Payroll Base Correction	
(line 27)	\$ 0.1 GF
SOA and University PERS increase	
(In operating budget for executive	
and legislative branches)	\$163.8 GF
Total Increase in FY 08 Governor's Budget	\$279.1 GF
Non-GF increases - Governor's Budget	\$ 62.0
Non-GF increases for other employers	\$ 2.1
PERS/TRS Estimated Costs (all sources)	\$698.1

TRS

Contributions estimated in FY 07 (all sources)	\$164.3
FY 08 Legislation and operating budget	
SB 52/HB 97 Education Bill	
Rate relief for school districts	
PERS/TRS contributions	\$170.5 GF
TRS Non-School Dist ER rate increase	
Relief (line 29)	\$ 0.5 GF
TRS School Dist. Payroll Base Correction	
(line 28)	\$ 1.7 GF
Transfer TRS increase funding from	
agencies to TRS DB plan:	
Education and Early Development	
(line 22 and 30)	\$ 1.0 GF
Labor and Workforce Development	
(line 23)	\$ 0.4 GF
University of Alaska (line 24)	\$ 13.3 GF

Total Increase in FY 08 Governor's Budget	\$187.4 GF
PERS/TRS Estimated Costs (all sources)	\$351.7
CSHB 97 amend TRS rate to normal cost	
Not reflected in operating budget	\$ 78.0 GF

Commissioner Kreitzer shared that this exhibit was intended to show "what everybody is paying". Most discussion would focus on how the cost share plan proposed in this legislation would affect budgets.

[9:33:17 AM](#)

Co-Chair Stedman interrupted to request more detail be provided on the aforementioned and forthcoming exhibits.

[9:34:01 AM](#)

Exhibit 1

Commissioner Kreitzer further explained this spreadsheet. She noted the FY 08 Board Requested rate for the State of Alaska would be 44.01 percent and the contribution would be \$373 million. If a pure cost share plan were adopted, the contribution rate for all employers would be 39.76 percent and the contribution amount for the State would be \$337 million, saving \$36 million. This data is listed for each employer.

[9:34:49 AM](#)

Co-Chair Stedman asked if the contribution rates include both normal costs and past service costs. He noted that the gross salary calculation for FY 08 was a three percent increase to FY 07 gross salary.

[9:35:14 AM](#)

Commissioner Kreitzer deferred to Ms. Millhorn.

[9:35:25 AM](#)

Ms. Millhorn explained that the normal cost, which pertains to the current expense, "in this particular case" is 14.48 percent. This is a consolidated normal cost for all PERS employers. Many of the FY 08 ARM Board requested rates are higher because past service costs are included. Past service costs are the costs of

the unfunded liability. The requested rate of 44.01 percent for the State of Alaska is comprised of 14.48 percent in normal costs and the remainder in past service costs. Past service cost is the unfunded liability amortized over 25 years. The normal cost rate of 14.48 percent could be subtracted from the Board requested rate for each employer to determine its past service cost.

[9:36:25 AM](#)

Co-Chair Stedman understood that the contribution rate would be 14.48 percent for those employers with no unfunded liability.

Ms. Millhorn affirmed.

[9:36:49 AM](#)

Senator Huggins deduced that those employers listed on the spreadsheet with a Board requested rate of 14.48 percent had no past service cost.

[9:37:06 AM](#)

Ms. Millhorn clarified that a provision included in the changes to the retirement system enacted through SB 144 in 2005, established a "floor" that would not allow employers' contribution rates be less than the normal cost. Therefore, the actual normal cost for some employers could be less than 14.48 percent.

[9:37:39 AM](#)

Co-Chair Stedman pointed out that several employers had a surplus and that those were mainly smaller communities, such as the City of Koyuk. He requested a listing of all communities with a surplus. The Committee would later discuss debt dilution and consideration for those communities with any surplus versus those with significant surplus.

[9:39:38 AM](#)

Co-Chair Hoffman understood that the Alaska Municipal League had supported the concept of a cost share plan. He asked if the Administration intended to present the details of the proposal

contained in this bill to the League and whether input would be considered.

[9:40:04 AM](#)

Commissioner Kreitzer answered that yes, the proposal would be detailed to the League. She acknowledged that not all employers would support the plan.

[9:40:28 AM](#)

Co-Chair Hoffman commented that the number of "losers" is more than the number of "winners". He anticipated the position of support could change.

[9:40:42 AM](#)

Commissioner Kreitzer responded that, as demonstrated in Exhibit 3, some of the employers could be "made whole" at a cost to the State of \$82 million. She compared this amount to the \$115 million proposed for rate relief currently under consideration in the FY 08 budget.

[9:41:01 AM](#)

Co-Chair Hoffman agreed, but countered that the \$82 million appropriation is only proposed for one year in this legislation.

[9:41:13 AM](#)

Commissioner Kreitzer informed that she had requested the Division of Retirement and Benefits to develop a plan to address the "out years".

[9:41:29 AM](#)

Ms. Millhorn continued outlining Exhibit 1, explaining the Gross Salary estimate for FY 08. The FY 08 Board Requested Rate includes the "level dollar amortization" and is applied to the Gross Salary estimate to determine the FY 08 contribution amount.

[9:42:31 AM](#)

Ms. Millhorn stated that the consolidated cost rate for all 186 employers would be 39.76 percent under a pure cost share system. Those amounts are listed for each employer in the next column. The last two columns list the increase or decrease respectively of each employer's contribution.

[9:43:16 AM](#)

Co-Chair Stedman remarked that the decreased amounts are not a savings on the liability, but rather is a "budgetary issue" in which the "cash flow call on the general fund" is reduced. The liability would remain.

[9:43:39 AM](#)

Ms. Millhorn affirmed that the pure cost share scenario reflected in this exhibit would not change the unfunded liability.

[9:44:00 AM](#)

Commissioner Kreitzer noted that \$25 million of the \$36 million State of Alaska "savings" is general fund. This proposal should be presented "holistically" because it involves multiple aspects.

[9:44:28 AM](#)

Co-Chair Hoffman asked whether the employee contribution rates would increase, as they would benefit from the retirement system.

[9:44:55 AM](#)

Ms. Millhorn responded that the contribution rate for employees would remain unchanged. These rates are established in statute as 7.75 percent for most public employees and 7.5 percent for peace officers.

[9:45:18 AM](#)

Co-Chair Hoffman asked whether the Administration had determined that employees should not contribute to the increases.

[9:45:40 AM](#)

Ms. Millhorn explained that the Alaska Constitution prohibits increases to existing employee contribution rates.

[9:46:13 AM](#)

Senator Elton asked the number of State and University of Alaska employees in comparison to employees of other members.

[9:46:34 AM](#)

Ms. Millhorn reported 33,000 active employees were currently enrolled in PERS, with approximately 14,500 of those State employees. She did not know the number of University employees enrolled in PERS.

[9:46:58 AM](#)

Co-Chair Stedman requested a table categorizing State and University employees and employees of other members delineated by headcount and by liability.

[9:48:16 AM](#)

Exhibits 2a and 2b

Commissioner Kreitzer stated that these spreadsheets show the impact of the cost sharing method and the proposed pension bond issuance for each employer. These figures are not intended to be exact, but rather provide a generalized overview.

[9:51:14 AM](#)

Exhibit 3

Commissioner Kreitzer noted that this spreadsheet follows the same format as the previous exhibits with the exception that it compares FY 07 to the proposal for FY 08.

[9:52:24 AM](#)

Co-Chair Stedman ordered the matter of pension obligation bonds be deferred for possible consideration as separate legislation.

[9:53:09 AM](#)

Commissioner Kreitzer referenced the fourth and final page of Exhibit 3, which lists the total increases between FY 07 and FY 08.

[9:53:50 AM](#)

Exhibit 4

Commissioner Kreitzer shared that this information was intended to assist in facilitating discussions on proposed changes in relation to the current status of the FY 08 operating budget legislation. The Department was "still trying to get a better figure" of the impact to the State and this table identifies the general fund costs. The information would continue to be updated to include all costs plus any additional items requested by the Committee.

Commissioner Kreitzer detailed the information on Exhibit 4.

[9:58:01 AM](#)

Commissioner Kreitzer qualified that as this information was being prepared, the House Finance Committee proposed a change to the TRS normal cost rate and thus the notation on the table.

[9:58:24 AM](#)

Exhibit 5a

PERS Cost Share

2005 Valuation Rate - Level Dollar Amortization

SOA takes 65% of 6/30/2005 Unfunded and issues \$1.7 billion in POBs

[Spreadsheet and flowchart combination detailing the Increase of FY 08 contribution amounts per ARMB set rates from FY 07 contribution amounts per ARMB set rates; Cost Share-05 Valuation rate-SOA takes 65%-\$1.7B POB, Cost Share contributions less original FY 08 contributions, and Relief to Employers whose cost share rate (31.86%)> orig FY 07 rate for two unspecified categories of Political Subdivisions, two unspecified categories of School Districts, SE Regional Resource Ctr and Spec Educ Service Agency. Also detailed are Original, Amend and Amended amounts associated with Legislation: SB 50 - Poli sub-Budget Bill, and SB 52 Education Bill. Impact on SOA from

OMB (excluding University) is listed as Post vacancy for General Fund, Fed, Other and Total Funding Source. These figures are totaled as follows.

Relief to Employers whose cost share rate (31.86%)> orig FY 07 rate	\$82,233,141
GF increase over orig 08 budget (per OMB) Rate from 44.01% to 47.92%	25,095,400
GF savings for University in 08 (per OMB) Rate from 33.75% to 31.86%	(2,542,600)
Total GF cost - revised	104,785,941
GF in SB 52 and SB 50 amended	115,409,583
GF added cost (savings) from proposal	(10,623,642)

A notation reads as follows.

Assumptions:

PERS goes to a cost share

State picks up 65% of 6/30/2005 unfunded liability

\$1.7 billion in POBs are issued 6/30/2007]

Commissioner Kreitzer detailed this information. She remarked that \$150 million is currently included in the proposed FY 08 operating budget for "rate relief". Of that amount, \$78 million is intended for political subdivisions and would be appropriated in SB 50 and the remaining \$38 million for school districts, the Southeast Regional Resource Center (SERRC) and the Special Education Service Agency appropriated in SB 52.

Commissioner Kreitzer then addressed the impacts of transition to a cost share plan. The cost share utilizing the FY 05 valuation rate with the State assuming 65 percent of the unfunded liability plus the issuance of \$1.7 billion in pension obligation bonds for political subdivisions would be \$136 million and \$79 million for school districts, SERRC and the Special Education Service Agency. The cost share contribution in the aforementioned circumstance less the currently proposed FY 08 State rate relief contributions would result in a savings of \$23 million for political subdivisions and \$10 million for the school district, SERRC and the Special Education Service Agency.

Commissioner Kreitzer continued outlining the cost to provide relief to those employers that would have an increased contribution rate under the cost share plan. That amount would be \$54,816,392 for political subdivisions and \$27,416,749 for school districts, SERRC and the Special Education Service

Agency. The total cost to hold harmless employers for FY 08 would be \$82,233,141 and is reflected in Exhibit 3 on page 14 of the handout.

Commissioner Kreitzer subtracted the \$150 million already included in the proposed budget for FY 08 from the total hold harmless cost to achieve a savings of \$10 million.

Commissioner Kreitzer clarified that these figures only pertain to the PERS system and do not include the TRS system.

[10:01:40 AM](#)

Exhibit 5b

Estimated TRS Contributions With Level Dollar Amortization
\$0.5 billion in cash, \$2 billion in POBs
[Spreadsheet listing the school districts that participate in TRS, the Department of Education and Early Development, SERRC, the Special Education Service Agency and the University of Alaska and the corresponding FY 07 Contribution Rate, FY 07 Estimated Contribution, FY 08 Board Adopted Rate, FY 08 Estimated Contribution, Total FY 08 increase over FY 07, FY 08 Rate after \$0.5B deposit and \$2B POB, FY 08 Contributions after \$0.5B deposit and \$2B POB, and FY 08 Contributions after \$0.5B deposit and \$2B POB in excess of original FY 08 Contribution.]

Commissioner Kreitzer reiterated that the previous exhibit pertained to PERS. This exhibit demonstrates the impact to employers of a \$.5 billion State appropriation and the issuance of \$2 billion in pension obligation bonds specific to TRS. She understood this is not included in the legislation before the Committee, but that it demonstrates the Administration plan to address retirement system funding issues.

Commissioner Kreitzer cautioned that pension obligation bonds "are not without risk". The most important "selling point" if the legislature were to decide to issue these bonds would be the benefit to the unfunded liability. The combined savings of such issuance over 25 years would total \$4 billion for both PERS and TRS.

[10:03:29 AM](#)

Commissioner Kreitzer understood the difficulty in addressing future needs with a limited amount of funding available.

[10:03:36 AM](#)

Exhibit 7a
State of Alaska
Public Employees' Retirement System
Employers who used SB 46 Rate Relief to pay down unfunded liability
Fiscal Year 2006

[Table listing those employers that utilized all or a portion of the State allocation intended to offset the contribution rate increase for the purpose of paying down that employers' unfunded liability. The amount of the appropriation and the amount applied to the unfunded liability for each employer are listed as follows.

Aleutians East Borough	\$50,537
Municipality of Anchorage	
Appropriation: \$6,615,843	
Amount applied to unfunded liability:	748,094
Bristol Bay Borough	70,944
City of Cordova	3,419
Denali Borough	29,484
City of Fairbanks	305,784
City of Galena	68,486
City of Kachemak	3,068
Ketchikan Gateway Borough	206,307
City of Ketchikan	415,937
City of Kodiak	293,700
Kodiak Island Borough	113,667
Lake and Peninsula Borough	32,811
City of North Pole	107,535
City of Palmer	132,967
City of Petersburg	198,490
City of Quinhagak	1,552
City of Seward	192,943
City of Soldotna	139,473
City of Tanana	11,285
City of Unalakleet	13,698
City of Valdez	255,619
City and Borough of Yakutat	22,773
Total applied to unfunded liability	\$3,517,055

A notation reads as follows:

In FY 05 the City of Soldotna paid an additional contribution of \$1 million to PERS to pay down their unfunded liability. Payment was made on March 10, 2005.]

Exhibit 7b

State of Alaska

Public Employees' Retirement System

Employers who used SB 231 Rate Relief to pay down unfunded liability

Fiscal Year 2007

[Table listing those employers that utilized all or a portion of the State allocation intended to offset the contribution rate increase for the purpose of paying down that employers' unfunded liability. The amount of the appropriation and the amount applied to the unfunded liability for each employer are listed as follows.

Aleutians East Borough	\$33,915
City of Bethel	
Appropriation: \$282,716	
Amount applied to unfunded liability:	275,716
City of Cordova	112,553
City of Egegik	2,830
City of Fairbanks	333,653
City of Huslia	5,215
Kenai Peninsula Borough	702,515
City of Ketchikan	400,460
Kodiak Island Borough	118,047
City of Kodiak	314,368
City of Palmer	154,333
City of Petersburg	206,671
City of Saxman	5,637
City of Seward	186,026
City of Soldotna	136,756
Total applied to unfunded liability	\$2,988,695

A notation reads as follows.

The following employers have not used their relief balances or requested it be used to pay down their unfunded liability. Any balance remaining at 6/30/07 will be used to pay down their unfunded liability. The Division last reminded employers of these balances and their options on 2/20/07.

City of Akutan	\$16,941
City of Allakaket	3,056
City of Atka	4,628
City of Barrow	47,355

Denali Borough	7,889
City of Fort Yukon	24,209
City of Galena	69,984
City of Homer	248,456
City of Hoonah	35,299
City of Hooper Bay	1,576
City of Kachemak	1,193
City of Kaltag	870
Ketchikan Gateway Borough	214,696
City of King Cove	50,001
City of Klawock	31,917
City of Koyuk	1,664
Lake and Peninsula Borough	19,656
City of Mountain Village	1,786
City of Nenana	12,244
City of Noorvik	12,352
Northwest Arctic Borough	44,779
City of Pelican	7,657
City of Quinhagak	1,920
City of Saint Paul	74,829
City of Sand Point	38,396
City of Seldovia	2,405
City of Skagway	89,301
City of Tanana	7,302
City of Thorne Bay	10,435
City of Unalakleet	11,157
City of Unalaska	520,772
Total	\$1,640,725

A notation reads as follows.

All other employers who received rate relief are using that relief to offset required contributions.

Commissioner Kreitzer suggested that the Committee's discussions could include consideration of these employers and the amount they would be required to contribute.

[10:04:11 AM](#)

Co-Chair Stedman requested further explanation of the two exhibits.

[10:04:18 AM](#)

Commissioner Kreitzer deferred to Ms. Millhorn.

[10:04:36 AM](#)

Ms. Millhorn stated that Exhibit 7a is a list of those employers that specifically applied to their portion of the unfunded liability, the five percent rate relief appropriated to all employers in FY 06. She exclaimed, "They are our heroes." She highlighted the City of Soldotna that applied their rate relief appropriation plus an additional \$1 million.

[10:05:39 AM](#)

Ms. Millhorn then explained that Exhibit 7b included a list of those employers that specifically did the same in FY 07. A second list shows those employers that had not specified that their rate relief appropriation be applied to their portion of the unfunded liability, but had not expended those funds either. If those employers take no affirmative action in expending the funds or directing the Department to apply the funds to the unfunded liability, those assets would eventually be automatically applied to their unfunded liability balance.

[10:06:56 AM](#)

Co-Chair Stedman commented that the additional appropriation by the City of Soldotna must have impacted its general fund and the delivery of goods and services. The Committee must devise a method in which to acknowledge these actions to ensure fairness.

[10:07:31 AM](#)

Commissioner Kreitzer anticipated this issue would receive further discussion. The proposed cost sharing plan would result in a \$10 billion savings, which could be utilized to accommodate these situations.

[10:07:54 AM](#)

Co-Chair Stedman asked whether the City of Soldotna was the only employer to contribute funds in addition to the State rate relief appropriation.

Commissioner Kreitzer and Ms. Millhorn indicated in the affirmative.

[10:08:17 AM](#)

Co-Chair Stedman continued that the matter of addressing debt dilution and compensating for employers that paid down their portion of the liability should be resolved in as fair a manner as possible.

[10:08:57 AM](#)

Commissioner Kreitzer continued her testimony as follows.

What we're proposing is a longer-term solution, rather than a fix that artificially lowers the employer contribution rate, but doesn't really impact the unfunded liability. To me, that's like paying only the interest on a credit card, instead of paying down the principal. Pension obligation bonds are not without risk. The Committee will hear from Department of Revenue representatives, if it chooses, about the risks and potential rewards. As part of our analysis of this approach, we've worked with our actuaries to come to the \$4.0 billion savings achieved by paying off the unfunded liability sooner rather than later.

In closing Mr. Chairman - I want to be sure to be clear on the record - Governor Palin comes from a municipal background, as you all know. Her concern is that we don't unduly burden local governments. We don't believe, when taken as a whole, this package does that. But, we're here to work with you, with the Legislature to craft a long-term solution. There will be some give and take in any solution, but we look forward to continuing the conversation.

[10:10:01 AM](#)

Co-Chair Stedman reiterated his intent to focus on the cost share issue and "clean up" of the provisions of the changes to the retirement system implemented by SB 141 and to not commingle the issue of pension obligation bonds. Once the liability was "cornered in the room" the discussion could continue to finding a solution.

[10:11:03 AM](#)

Senator Elton pointed out that Exhibits 1 through 5 showed the average rate based on the FY 05 valuation. However, the

provisions of Section 7 of the bill utilized the FY 06 valuation as the base. He questioned the discrepancy.

[10:12:02 AM](#)

Ms. Millhorn gave the following response.

Section 7, the allocation of the 65 percent is as of June 30, 2006. That's the projected. That includes the experience study. So that looks at the assignment of 65 percent of the liability to the State of Alaska of approximately \$3.5 or \$3.6 billion compared to the valuation. The valuation as of June 30th of 2005, the State of Alaska is at 57 percent and its \$2.5 billion. So this contemplates that that's the projected amount for the valuation for June 30th of 2006, which is the higher amount at 65 percent.

[10:12:54 AM](#)

Senator Elton again asked why if the FY 05 valuation was utilized in the legislation, the FY 06 valuation was utilized in the exhibits. He asked if the exhibits were amended to reflect the valuation of June 30, 2006 whether the calculated amounts would change.

[10:13:26 AM](#)

Ms. Millhorn answered that completed valuations for June 30, 2006 were not finalized. The ARM Board has adopted the employer contribution rates based on the June 30, 2005 valuations. The provisions of Section 7 of the bill would assign a portion of the unfunded liability to the State based on the last available valuation from 2005. The Division's chief financial officer has collaborated with the actuary to devise the projected valuation of the unfunded liability. This amount of \$8.6 billion has been discussed in this Committee and is based on the experience study. The unfunded liability of PERS is \$5.5 billion and "under the valuation" the amount is \$4.4 billion.

[10:14:36 AM](#)

Co-Chair Stedman asked the date the valuation as of June 30, 2006 would be available.

[10:14:46 AM](#)

Ms. Millhorn replied that the projected completion date is June 2007.

[10:14:51 AM](#)

Commissioner Kreitzer interjected that the intent of utilizing the projected 2006 valuation data was to "take the known and be able to run these scenarios and then take the worst case scenario, which we know is coming, and put it in the bill." The information contained in the exhibits is "the best we can give you right now to understand the impact of what we're proposing."

[10:15:13 AM](#)

Senator Elton asked why the known valuations from June 30, 2005 were not utilized in the legislation.

[10:15:45 AM](#)

Commissioner Kreitzer answered that the older valuation data could be utilized; however, the intent is to not "ignore" that the unfunded liability is continuing to increase.

[10:16:05 AM](#)

Co-Chair Stedman spoke to the issue of the two-year "lag time" in securing valuation figures. At the end of the fiscal year, studies are conducted and upon completion are forwarded to the ARM Board for use in setting employer contribution rates. The ARM Board is attempting to accelerate this process. This delay is partially the cause of the current situation involving the significant unfunded liability.

[10:17:00 AM](#)

Senator Elton stressed the difficulty for municipal governments to budget for their contribution before the amount was known. He analogized this to "shooting in the dark".

[10:17:32 AM](#)

Co-Chair Stedman intended to conduct a "sensitivity analysis" to compare the proposed assumption of 65 percent of the unfunded

liability by the State and 35 percent by the other employers, to other ratios, including 60:40 and 70:30.

[10:18:10 AM](#)

Co-Chair Hoffman asked if the proposed contribution rates would apply to both defined benefits and defined contribution employees.

[10:18:28 AM](#)

Ms. Millhorn replied that this legislation would apply to the defined benefit plan. This bill does include a provision that would include the defined contribution plan "for purposes of liquidating the past service liability."

[10:18:52 AM](#)

Co-Chair Hoffman asked the estimated savings that would be achieved over time through attrition, as no new employees would be added to the defined benefit plan.

[10:19:05 AM](#)

Ms. Millhorn explained that "in this case" the "payroll amount will be spread over both the DB [defined benefit] and the DCR [defined contribution]" according to a calculation based on the amount necessary to "liquidate" the unfunded liability. This would stabilize the rate and the amount received into the retirement system. If the payroll rate were used only for the DB members, that rate would have to increase. However, the contribution rate to the DCR members would not "really change".

[10:20:26 AM](#)

Co-Chair Stedman directed attention to Section 10, which would "remove the ability of the employer to amend the participation agreement and allow only for termination of the plan." He commented on the "surprise" to most communities, that the calculation performed by the actuary would be higher if that employer chose to terminate from participation in the PERS plan. He gave the community of Ruby as an example.

[10:21:06 AM](#)

Ms. Millhorn responded that in the event an employer terminated its participation agreement, each employee is given the right to "vest or refund out of the plan". The termination costs would be based on the individual election of the employees of that employer. She gave an example of a "small employer" with 25 employees, in which several of those employees had less than five years of service and elected to refund from the system. In this instance, the termination cost would be lowered. If however, those individuals elect to vest in the system, the employer costs would be higher. The primary factor impacting the termination rate is the associated medical costs, which could make a "huge difference" to the employer. The actual amount would be based on the number of years each employee had served.

[10:22:46 AM](#)

Co-Chair Hoffman asked if a transition period would be provided to allow employers to remain in the plan or terminate from participation.

[10:23:06 AM](#)

Ms. Millhorn replied that employers would have the ability to voluntarily terminate from the plan at any future date. However, an employer that terminated would be required to pay the termination costs, which would include the analysis of the costs for those employees who elected to vest in the plan.

[10:23:37 AM](#)

Co-Chair Hoffman asked if the termination costs would also be levied on those employers characterized in the exhibits as "losers" who would experience increased contribution rates for remaining in the plan. He contended that differentiation should be made on this matter between the "winners" and the "losers".

[10:23:57 AM](#)

Commissioner Kreitzer expressed wiliness to continue to discuss these options. A significant factor would be how the final legislation accommodates for winners and losers.

[10:24:25 AM](#)

Senator Olson asked the number of communities currently in this "dilemma" in attempting to reduce their budget and "caught in this situation".

[10:24:45 AM](#)

Commissioner Kreitzer answered that the Department has determined that if the PERS system were converted to a pure cost share plan, those communities listed in Exhibit 2b as losers could face this situation. However, the Administration's proposal would be to make those employers whole for FY 08 and to develop a method that would "smooth out" for future years. She intended to speak to the Alaska Municipal League on this issue.

[10:25:40 AM](#)

Senator Olson asked if about any "relief in sight" that could be provided to those employers charged termination costs for terminating participation in the PERS plan as a result of the changes made in this legislation.

[10:26:07 AM](#)

Commissioner Kreitzer had not reviewed the matter to determine the number of communities that could chose to terminate for existing reasons versus those that could terminate as a result of the adoption of a cost share plan. She would report on her findings.

[10:26:29 AM](#)

Co-Chair Stedman identified the issue of the impact to those communities with a surplus or a "small liability". "Pinpointing" the exact "asset liability spread" of all employers would be difficult.

[10:27:11 AM](#)

Senator Elton referred to earlier testimony stating that this proposal is similar to the transition of the TRS system to a cost share plan. He asked if any provisions in this legislation were unique to the PERS system and not identical to the TRS cost share plan.

[10:27:36 AM](#)

Commissioner Kreitzer answered that Senator Huggins had posed a similar question and had requested the Department to provide a comparison of the elements of TRS to the proposed PERS plan. She asked if this would be sufficient to Senator Elton's needs.

[10:27:56 AM](#)

Senator Elton affirmed.

[10:28:11 AM](#)

Co-Chair Stedman announced that public comment on this legislation would be forthcoming. Additional discussion would be held on issues raised at this hearing; however, pension obligation bonds would not be considered as part of the debate.

[10:28:58 AM](#)

Senator Huggins cautioned against release of insufficient or incorrect information to the public. This occurred with the passage of SB 141 and resulted in misunderstanding of the implications of that change to the retirement systems. He advised the Administration to be "up front" with all aspects of the process relating to the current proposal.

[10:29:27 AM](#)

Commissioner Kreitzer expressed intent to "stay out in front" of any misinformation, noting the Department would post all exhibits and data on its website in one attempt to accomplish this.

[10:30:04 AM](#)

Co-Chair Stedman encouraged those wanting to testify on this bill to contact his office for scheduling purposes.

AT EASE [10:30:19 AM](#) / [10:30:38 AM](#)

#

ADJOURNMENT

Co-Chair Bert Stedman adjourned the meeting at [10:31:14 AM](#)