

ALASKA STATE LEGISLATURE
HOUSE COMMUNITY AND REGIONAL AFFAIRS STANDING COMMITTEE

March 28, 2013

8:06 a.m.

MEMBERS PRESENT

Representative Gabrielle LeDoux, Co-Chair
Representative Benjamin Nageak, Co-Chair
Representative Neal Foster
Representative Bob Herron
Representative Kurt Olson
Representative Lora Reinbold
Representative Harriet Drummond

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

HOUSE BILL NO. 174

"An Act requiring each municipality with a population that decreased by more than 25 percent between 2000 and 2010 that participates in the defined benefit plan of the Public Employees' Retirement System of Alaska to contribute to the system an amount calculated by applying a rate of 22 percent of the total of all base salaries paid by the municipality to employees of the municipality who are active members of the system during a payroll period; reducing the rate of interest payable by a municipality with a population that decreased by more than 25 percent between 2000 and 2010 that is delinquent in transmitting employee and employer contributions to the defined benefit plan of the Public Employees' Retirement System of Alaska; giving retrospective effect to the substantive provisions of the Act; and providing for an effective date."

- HEARD & HELD

PREVIOUS COMMITTEE ACTION

BILL: HB 174

SHORT TITLE: PERS CONTRIBUTIONS BY MUNICIPALITIES

SPONSOR(s): COMMUNITY & REGIONAL AFFAIRS

03/18/13	(H)	READ THE FIRST TIME - REFERRALS
03/18/13	(H)	CRA, L&C

03/28/13

(H)

CRA AT 8:00 AM BARNES 124

WITNESS REGISTER

PAUL LABOLLE, Staff
Representative Foster
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: On behalf of the sponsor, provided further information on HB 174.

MIKE BARNHILL, Deputy Commissioner
Department of Administration
Juneau, Alaska

POSITION STATEMENT: During hearing of HB 174, answered questions.

KATHIE WASSERMAN, Executive Director
Alaska Municipal League (AML)
Juneau, Alaska

POSITION STATEMENT: Testified in support of HB 174.

GREG MOYER, Interim City Manager
City of Galena
Galena, Alaska

POSITION STATEMENT: During hearing of HB 174, explained the situation that has left Galena with a salary floor it can't meet.

BROOKS CHANDLER, Attorney, Partner
Boyd, Chandler & Falconer, LLP
Anchorage, Alaska

POSITION STATEMENT: As the attorney for the City of Galena, testified on HB 174.

ACTION NARRATIVE

[8:06:57 AM](#)

CO-CHAIR BENJAMIN NAGEAK called the House Community and Regional Affairs Standing Committee meeting to order at 8:06 a.m. Representatives Herron, Reinbold, Foster, Drummond, LeDoux, and Nageak were present at the call to order. Representative Olson arrived as the meeting was in progress.

HB 174-PERS CONTRIBUTIONS BY MUNICIPALITIES

[8:07:46 AM](#)

CO-CHAIR NAGEAK announced that the only order of business would be HOUSE BILL NO. 174, "An Act requiring each municipality with a population that decreased by more than 25 percent between 2000 and 2010 that participates in the defined benefit plan of the Public Employees' Retirement System of Alaska to contribute to the system an amount calculated by applying a rate of 22 percent of the total of all base salaries paid by the municipality to employees of the municipality who are active members of the system during a payroll period; reducing the rate of interest payable by a municipality with a population that decreased by more than 25 percent between 2000 and 2010 that is delinquent in transmitting employee and employer contributions to the defined benefit plan of the Public Employees' Retirement System of Alaska; giving retrospective effect to the substantive provisions of the Act; and providing for an effective date."

[8:08:29 AM](#)

REPRESENTATIVE FOSTER, speaking as the sponsor of HB 174, informed the committee that HB 174 seeks to correct an unintended consequence of the salary floor enacted in 2008 by Senate Bill 125 in the 25th Alaska State Legislature. The salary floor was meant to prevent Public Employees' Retirement System (PERS) employers from gaming the system by laying off PERS employees and hiring contract employees to reduce their contribution to the system. [The salary floor] was not meant to saddle communities experiencing an exodus event with a financial burden that can't possibly be administered. Therefore, HB 174 removes the 2008 salary floor for communities that lost more than 25 percent of their population between the 2000 and 2010 census period. For those communities, the interest rate on delinquent payments is reduced from 22 percent to either a rate agreed upon with the administration or three percentage points above the Federal Reserve discount rate for the applicable payroll period.

[8:09:46 AM](#)

PAUL LABOLLE, Staff, Representative Foster, Alaska State Legislature, explained that by narrowing the legislation to only those communities that lost 25 percent of their population, it would only refer to the following five communities: Galena, Atka, Pelican, Anderson, and St. George. Since Anderson and St. George don't currently have any PERS eligible positions they are

included within the scope of the legislation as a matter of law, but not practically. He then noted that he wasn't sure if Atka is even a functioning community. Therefore, Pelican and Galena are the communities that will be directly impacted by HB 174. In the way of background, Mr. LaBolle explained that Senate Bill 125 was a way to bail out the PERS system. In the past, each municipality was responsible for its own retirement system under PERS, and therefore the system's benefits were laid out by statute while the actual management of that system was up to each municipality. Senate Bill 125 turned the aforementioned into a pooled resource such that every community is in the same system. A large amount of funds were provided by the state to help secure the unfunded liability while at the same time there was the desire to ensure municipalities paid their fair share. The concern, he explained, was that municipalities would lay off employees in order to reduce the number of PERS positions on which they would be paying into the system and hire contract employees to perform the same task. Unfortunately, exodus events in certain communities weren't foreseen. A community that loses more than 25 percent of its population won't carry the same amount of municipal staff. For Galena, there is an unfunded liability of almost \$500,000 for a population of 500, and thus there is no way to carry that [unfunded liability]. Since the aforementioned wasn't the intent of Senate Bill 125, HB 174 offers a targeted approach to rectify the situation.

[8:12:49 AM](#)

CO-CHAIR LEDOUX asked whether these communities are behind in their payments with what she characterized as a very high rate of interest.

MR. LABOLLE replied yes, and added that Galena is delinquent and faces a 22 percent interest rate. Section 2 addresses interest rates for delinquent communities that fall within the definition [provided under HB 174].

[8:13:38 AM](#)

CO-CHAIR LEDOUX surmised then that HB 174 wouldn't reduce the interest rate for other communities that are delinquent and asked whether there are other communities that are delinquent.

MR. LABOLLE replied yes.

[8:14:04 AM](#)

REPRESENTATIVE FOSTER stressed that the assumption when [Senate Bill 125 passed] was that communities would grow, and thus they wouldn't have a problem with the payments as they would add employees into the system.

[8:15:24 AM](#)

MIKE BARNHILL, Deputy Commissioner, Department of Administration, said that he has a spreadsheet of delinquent communities as of January 31, 2013, but Pelican isn't on that delinquent list.

[8:15:54 AM](#)

CO-CHAIR LEDOUX asked if all the delinquent communities are paying 22 percent.

MR. BARNHILL replied no, recalling that the rate of interest is 12 percent. The interest rate is the earnings assumption of the system, 8 percent, plus another 50 percent of that, 4 percent, which totals 12 percent.

CO-CHAIR NAGEAK opened public testimony.

[8:16:38 AM](#)

REPRESENTATIVE OLSON inquired as to whether 8 percent is overly optimistic.

MR. BARNHILL noted that there is a debate in the pension, actuarial, and economist communities regarding whether 8 percent for a public pension system is overly optimistic. The majority of pension systems have adopted 8 percent or something in the range of 8 percent. A Chicago economist, he related, believes 8 percent is very optimistic and recommends a riskless rate of return in the range of 4-5 percent. If the [Alaska Retirement Management (ARM)] Board adopted a more riskless rate of return that would essentially double the unfunded liability of the systems. Currently, the total unfunded liability for the systems is \$11.9 billion, which would place pressure on the state assistance payments that the legislature appropriates every year. Mr. Barnhill acknowledged that a lengthy discussion on the choice to use 8 percent could be held, but said that for now 8 percent is in the range of prudent and it's possible that the ARM Board will consider rate reductions in the future.

[8:18:12 AM](#)

REPRESENTATIVE OLSON conjectured that 8 percent is what placed [the state] in the situation it is now [with the PERS unfunded liability].

MR. BARNILL responded that a number of issues resulted in the state's current situation with the [PERS unfunded liability]. Certainly, one of those issues is not targeted the assumed rate of return. Over the past 5 years, the rate of return has been well below 8 percent a year. Going forward, the investment advisor for the ARM Board has indicated there is practically no likelihood that 8 percent will be reached in the next 10 years.

[8:19:04 AM](#)

CO-CHAIR LEDOUX inquired as to the average rate of return over a 20-year period.

MR. BARNHILL offered to provide that information to the committee.

CO-CHAIR LEDOUX questioned the choice of 8 percent if the assumed rate of return hasn't been 8 percent over the last 20 years, now, and little hope reaching it over the next five years.

MR. BARNHILL reminded the committee that there are boom and bust markets, and therefore there is at least one slice during which the average rate of return was in excess of 8 percent. He noted that per statute the ARM Board is required to provide the legislature 1-, 4-, 7-, and 10-year average rate of returns.

[8:20:31 AM](#)

REPRESENTATIVE HERRON referred to the sponsor statement, which relates that the salary floor was instituted to ensure that the system couldn't be gamed. However, he questioned whether the system is being gamed anyway because of the high expectation of the ARM Board.

MR. BARNHILL said that the ARM Board adopts many assumptions, the point of which in a defined benefit system is to attempt to project the savings necessary in order to pay defined benefits in the future. In addition to the earnings reserve assumptions, there are assumptions for mortality, retirement, medical expenses, health care cost growth, and inflation. He said he could guarantee that one or more of those assumptions about the

future will be incorrect, which is the nature of a defined benefit plan. By statute and guaranteed by the constitution, the state has committed to pay certain defined benefits in the future. The only way to achieve the aforementioned is to make assumptions regarding what the future holds in order to save money and invest it.

[8:22:17 AM](#)

REPRESENTATIVE OLSON requested the average rate of return reports from the ARM Board.

MR. BARNHILL agreed to provide those.

[8:22:51 AM](#)

KATHIE WASSERMAN, Executive Director, Alaska Municipal League (AML), said that the municipalities understand the huge liability faced with the PERS liability and appreciate the agreement between the state and PERS employers to settle on 22 percent of the past service cost and the present service cost. However, some municipalities just can't pay this kind of penalty on losing employees due to a decrease in population. The [PERS salary floor] has taken away their ability to manage their employees and their city. She recalled that originally Galena's bill was about \$129,000, but with the 12 percent interest it has now grown to about \$500,000. The original amount was very difficult to impossible for Galena while \$500,000 is impossible. Ms. Wasserman provided an example with the City of Pelican that she recalled having a population/tax base of 150 people that decreased to 62 people. In such situations, [reductions/layoffs] have to occur and that incurs a cost of its own. Therefore, AML supports HB 174 as there has to be some relief for these smaller communities. Although the larger municipalities are probably in a better position to game the system, they are also in a better position to be able to pay penalties. With regard to gaming, Ms. Wasserman didn't believe the smaller communities, which aren't close to main population areas, would know how to game the system.

[8:25:51 AM](#)

REPRESENTATIVE HERRON inquired as to the alternative for Galena if HB 174 doesn't make it this legislature.

MS. WASSERMAN surmised that it would be in the state's hands.

[8:26:24 AM](#)

REPRESENTATIVE HERRON, appealing to Ms. Wasserman being a former city manager, inquired as to what she would recommend to her community.

MS. WASSERMAN recalled that for a community to dissolve it must fill out a petition, which requires enough work that the community, particularly smaller ones, would have to hire a consultant. However, it's probably not worth it for those on the brink of dissolving to hire a consultant for a year petition system. Therefore, she would suggest mailing the key to the city hall to the state.

[8:27:33 AM](#)

REPRESENTATIVE DRUMMOND inquired as to why other communities listed on the chart as having had employees that don't now aren't included in the bail out.

MR. LABOLLE clarified that the chart doesn't show the population percentage but rather shows the salary floor. Communities could be impacted by the salary floor for any number of reasons, including loss of employees or lowering of the salary base.

[8:28:47 AM](#)

MR. LABOLLE explained that in 2008 Senate Bill 125 took a snapshot of that fiscal year and said that going forward the community's contribution will be 22 percent of the current salary base or 22 percent of the 2008 salary base, whichever is more. As mentioned earlier, when populations increase, salaries increase and thus the salary floor shouldn't be an issue.

[8:29:33 AM](#)

REPRESENTATIVE OLSON requested the list of the communities with their populations and change in population. Representative Olson expressed concern that [HB 174] may create a situation in which there are a number of communities that fall just outside the current parameters and the legislation could "Christmas tree."

MR. LABOLLE deferred to Mr. Barnhill, DOA. He reminded the committee that the communities that fall within the definition in HB 174 are Galena, Pelican, Atka, Anderson, and St. George. However, Anderson and St. George don't currently have any

eligible PERS positions, and thus aren't functionally a part of HB 174. Furthermore, the legislation defines the population loss within the 2000 and 2010 census period and anything occurring beyond that census period would be applicable under the definition in HB 174.

[8:30:48 AM](#)

REPRESENTATIVE OLSON clarified that his point is that the legislation has an arbitrary line that could be changed in the next committees of referral to include those communities that fall just outside of the existing definition in HB 174. Therefore, it would be helpful to know which communities fall just outside of the definition in HB 174.

[8:31:32 AM](#)

REPRESENTATIVE HERRON opined that the danger is that the legislation is being pre-loaded, which is why it's necessary to further analyze it.

[8:32:11 AM](#)

GREG MOYER, Interim City Manager, City of Galena, informed the committee that 11 months ago he was hired to restructure and ultimately save Galena, which is still reeling from the 2008 closer of the Galena Air Base. He opined that the military became Galena's economic engine as it provided residents, jobs, and economic stability. In 1994, the Galena airbase was realigned in 1994 and its population fell from 800 to 650, which was a 20 percent reduction. In 2005, the Base Realignment and Closure (BRAC) Commission decided to move forward with the closure of the Galena Air Base by September 2008, which is the same time the state took the snapshot of Galena's salaries that required that salary floor be met every year or Galena would be penalized by 22 percent of the difference plus interest. As has been mentioned, Galena's population is just below 500 now. Mr. Moyer told the committee that he developed an austere fiscal year (FY) 2013 budget with total PERS salaries in the amount of about \$800,000. Unfortunately, those PERS salaries are over \$600,000 less than the state's salary floor. That 2008 salary snapshot is \$1.5 million, which must be met every year. Galena is being charged 22 percent of the difference, approximately \$139,000 every year plus interest. Galena, he stressed, will never meet its salary floor amount. He further stressed that there is no gaming in Galena. Mr. Moyer acknowledged that he has the option to add 15-20 positions or give existing employees

a raise. He then pointed out that current law leaves no room for DOA to consider hardships. Therefore, Mr. Moyer requested a legislative fix for this situation that developed through no fault of Galena. In conclusion, Mr. Moyer emphasized the need for a common sense solution and reiterated that there is no gaming on the part of Galena.

[8:37:19 AM](#)

BROOKS CHANDLER, Attorney, Partner, Boyd, Chandler & Falconer, LLP, speaking as the attorney for the City of Galena, pointed out that the salary floor in 2008 was created as a disincentive for municipal employers to bail out of PERS due to the increase in the contribution rate to 22 percent. The overall policy of the salary floor isn't impacted by HB 174, which recognizes that a one-size-fits-all statewide policy has unintended and unduly punitive consequences in that salary decreases due to population decreases is out of the control of these communities. The solution proposed in HB 174 is very focused, narrow, and limited to communities with a population loss that existed between the 2000 and 2010 census and provides an alternative contribution rate that isn't fixed on what salaries were in 2008 but rather existing salaries.

[8:39:37 AM](#)

REPRESENTATIVE HERRON questioned whether a new snapshot should be taken.

[8:40:06 AM](#)

CO-CHAIR NAGEAK announced that HB 174 would be held over.

[8:40:36 AM](#)

ADJOURNMENT

There being no further business before the committee, the House Community and Regional Affairs Standing Committee meeting was adjourned at 8:40 a.m.