

HOUSE FINANCE COMMITTEE

April 12, 2014

2:54 p.m.

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CALL TO ORDER

Co-Chair Stoltze called the House Finance Committee meeting to order at 2:54 p.m.

MEMBERS PRESENT

Representative Alan Austerman, Co-Chair  
Representative Bill Stoltze, Co-Chair  
Representative Mark Neuman, Vice-Chair  
Representative Mia Costello  
Representative Bryce Edgmon  
Representative Les Gara  
Representative David Guttenberg  
Representative Lindsey Holmes  
Representative Cathy Munoz  
Representative Steve Thompson  
Representative Tammie Wilson

MEMBERS ABSENT

None

ALSO PRESENT

Angela Rodell, Commissioner, Department of Revenue; Michael Barnhill, Deputy Commissioner, Department of Administration; Gary Bader, Chief Investment Officer, Treasury Division, Department of Revenue; David Teal, Director, Legislative Finance Division; Karen Crane, Alaska Municipal League; Pat Branson, Mayor, Kodiak; Larry DeVilbiss, Mayor, Mat-Su Borough; Bob Bartholomew, Finance Director, City and Borough of Juneau; Senator Fred Dyson; Joshua Banks, Staff, Senator Dyson; Commissioner Schmidt, Department of Corrections; Leslie Houston, Deputy Commissioner, Department of Corrections; Dan DeBartolo, Director, PFD Division, Department of Revenue.

PRESENT VIA TELECONFERENCE

Mim McConnell, Mayor, City of Sitka; John Sweeney, Finance Director, City of Sitka; Rick Kock, City Manager, Kenai; Jennifer Johnston, Anchorage Assembly, Alaska Municipal League, Anchorage; Jim Williams, Chief of Staff, City of Fairbanks; Sallie Stuvek, Human Resources Director, Fairbanks North Star Borough; Jon Bolling, City of Craig; Stephanie Scott, Mayor, Haines Borough.

SUMMARY

HB 349 AK RETIREMENT RESERVE FUND

HB 349 was SCHEDULED but not HEARD.

HB 385 PERS/TRS STATE CONTRIBUTIONS

HB 385 was HEARD and HELD in committee for further consideration.

CSSB 104(FIN)

APPROPRIATIONS FROM THE DIVIDEND FUND

CSSB 104(FIN) was HEARD and HELD in committee for further consideration.

CSSB 194(FIN)

TOURISM MARKETING BOARD

CSSB 194(FIN) was SCHEDULED but not HEARD.

CSSB 195(FIN)

POSTSECONDARY EDUCATION LOANS/GRANTS

CSSB 195(FIN) was SCHEDULED but not HEARD.

#hb385

HOUSE BILL NO. 385

"An Act relating to additional state contributions to the teachers' defined benefit retirement plan and the public employees' defined benefit retirement plan; and providing for an effective date."

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ANGELA RODELL, COMMISSIONER, DEPARTMENT OF REVENUE, introduced the Public Employees' Retirement System (PERS)

and Teachers Retirement System (TRS) funding solution legislation. She understood that legislators also worked diligently to arrive at a solution for the state's unfunded liability weighing the long-term financial impact against other demands on the state's resources.

Commissioner Rodell remarked that pension funding was an issue for many years. She recounted that the issue was addressed in November 2010 by the Alaska Retirement Management Board (ARMB) and a number of different options were considered. She stated that in September 2011, the governor asked the ARMB to seek potential solutions. In 2012, the ARMB adopted the "level dollar" approach; the lowest cost option in the long-term. Within two years, the actuarial reports revealed the long-term budget impact of the approach, which prompted further examination. The actuarial reports exposed the "real value" in the level dollar approach in terms of lower costs, but the administration also understood the real value in creating "budget certainty and budget durability." She underlined that the solution was a compromise between the level dollar approach and initially pre-funding a portion of the liability and creating budget certainty with an ongoing payment.

MICHAEL BARNHILL, DEPUTY COMMISSIONER, DEPARTMENT OF ADMINISTRATION, discussed the Power Point Presentation: "PERS/TRS Funding Solution, Governor Sean Parnell" (copy on file). He reported that the first several slides provided background information on the issue. He began with Slide 3 and explained that the defined benefit pension system was administered by three entities:

"Organization"

- 1) Department of Revenue  
Treasury Division  
Invests retirement system assets
- 2) Alaska Retirement Management Board  
Sets contribution rates, invests retirement system assets.
- 3) Dept. of Administration  
Division of Retirement & Benefits  
Administers retirement and benefits system.

Mr. Barnhill expounded that the retirement system assets amounted to \$20 billion and the defined contribution assets

were approximately \$5 billion. He added that the ARMB had nine members appointed by the Governor comprised of PERS and TRS employees, two public members, one municipal finance officer, and two commissioners. The Department of Administration (DOA) administered the pension and health care benefits which amounted to \$1.5 billion per year.

Mr. Barnhill continued with slide 4: "Membership." The slide depicted a chart containing the membership statistics as of December 31, 2013. He highlighted that the state employed 27,000 active members of PERS and TRS and had 42,000 retirees. Including dependents approximately 120,000 people were encompassed under PERS and TRS plans.

Mr. Barnhill discussed slide 5: "Benefits." The graph depicted the projected benefits payments. The system was projected to pay \$136 billion in benefits by 2070. He reported that the current PERS/TRS account balance was \$19.9 billion. [The unfunded liability reported on the slide amounted to approximately \$11.9 billion.]

Mr. Barnhill discussed slide 6:

#### Defined Benefits

Defined Benefit Pension: fixed benefit amount from date of retirement to death

Contributions + Investment Earnings = Benefits + Expenses

IF

Experience equals actuarial assumptions

Actuarial Assumptions:

Inflation, Investment Return, Mortality, Date of Retirement, Cost of Healthcare, Payroll Growth, Disability, Spouse Age, Dependent Children, COLA, Plan Expenses, Turnover

Experience that falls short of projections leads to unfunded liability

Employer Takes the Risk

Mr. Barnhill informed the committee that the critical piece of the defined benefit formula was investment earnings. The state's active employees contributed 6.75 percent to 8.75

percent of their salary to the plan. The actuary set the rates each year for the amount the employer needed to contribute. The rates were highly unstable since 2002. The current balance determined the rates; set at 12 percent for TRS and under 10 percent for PERS. In addition, health care cost projections were not satisfactory. Employer contribution rates rose dramatically since the early 2000's. The projected FY 15 employer contribution rate was over 40 percent for PERS and over 70 percent for TRS. He elaborated that two types of costs or rates were included in a defined benefit system. The normal cost was the rate collected from employees and employers. Nothing additional was necessary beyond the normal cost if all actuarial assumptions were correct. The actuarial projections were not correct and were underestimated over the last 10 years. The underestimated contributions were known as a "past service liability" and a past service liability contribution rate was established by the actuarial. He emphasized that when the actuarial underestimates the employer takes the risk. The situation lead to the current challenge for the state of how to manage the unfunded liability.

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Mr. Barnhill turned to slide 7: "Events."

2002 - Milliman actuarial audit; dotcom collapse  
2003 - FY 2002 valuations released with revised assumptions.  
\$4.1B unfunded liability  
2005 - SB 141 enacted: DB plans closed; DC plans created; PERB/TRB/ASPIB sunset; ARM Board created  
2007 - ARM Board files suit against Mercer for actuarial negligence; SB 123 enacted: PERS cost share  
2008 - SB 125 enacted: employer contribution rates capped; state assistance begins; Great Recession begins  
2009 - PERS / TRS investment loss: (20.5%)  
2010 - Mercer litigation settled for \$500mm (net \$403mm); other states begin to cut DB benefits, change plans;  
2012 - ARMB adopts level dollar amortization; \$11.9B unfunded liability  
2013 - 12.5% investment gain; recession over?

Mr. Barnhill summarized that throughout the 1990's the impact of growing healthcare costs were underestimated and the collective downturn in the investment market in the early 2000's and again in 2009 were the largest drivers of the current unfunded liability of \$11.9 billion.

Mr. Barnhill moved to slide 8: "PERS/TRS Balance Sheet." He explained that an 80 percent funding ratio was a common gauge for a healthy system. Both PERS (61.3 percent) and TRS (52.1 percent) were well under the 80 percent funding ratio which indicated additional funding was needed. The total balance for both accounts was approximately \$20 billion.

Mr. Barnhill addressed the graphs on Slides 9 and 10. He believed that the state appropriated "extraordinary" amounts on behalf of public employees and school districts each year. The current year contribution totaled \$3.3 billion; \$1.7 was appropriated on behalf of school districts and \$1.6 billion for state and municipal employees. He questioned whether school districts could have existed without the state's contributions.

Mr. Barnhill discussed the multiple approaches to deal with the unfunded liability. He discussed Slide 9: "PERS/TRS Approaches to Unfunded Liability." He noted that ARMB amortized the unfunded liability over 25 years at the "level percentage of pay" methodology. The payments on the unfunded liability were expected to grow at the same rate as payroll would grow (approximately 4 percent). He termed the system as a "back loaded" amortization methodology and defined it as a system where contributions were less in earlier years and increased in later years in nominal dollar terms. He noted that slide 9 illustrated the trend, depicting payments ranging from \$700 million per year currently and increasing to well over \$2 billion per year in the late 2020's. The ARMB considered the payment methodology with dozens of scenarios with the goal of paying it down in an affordable way.

Mr. Barnhill discussed slide 10: "PERS/TRS Approaches to Unfunded Liability." The ARMB adopted a new methodology for amortizing the unfunded liability called "Level Dollar." He delineated that level dollar was formula based and identical to home mortgage amortization with equal flat level payments over the amortization period; referred to as a "front loaded" amortization methodology. He pointed out

that the profile of the graph curve from FY 2015 through FY 2030 depicted higher payments earlier and lower payments later. If adopted the payments would go from \$630 million in FY 2014 up to \$975 million in 2015 and would crest over \$1 billion in FY 2016 through FY 2020 and begin to trend down. The main concern was finding consensus on what amount was affordable. He thought that the general consensus was that multiple billion dollar payments were not affordable. The administration searched for a more affordable way of responsibly amortizing the unfunded liability in the next several years.

GARY BADER, CHIEF INVESTMENT OFFICER, TREASURY DIVISION, DEPARTMENT OF REVENUE, announced that that the benefits were secure today, but unless addressed soon, the combination of increased benefits and insufficient investments impacted the rate of return, leading to reduced earnings and increased contributions. He turned to slide 12:

#### Fund Liquidity Analysis

Although there is a substantial unfunded liability in both the PERS and TRS, there are billions of dollars to pay benefits well into the future.

Benefits payments will increase substantially in the next decade. Unless addressed, the combination of increased benefit payments and insufficient assets in the trusts will require investing in more liquid assets.

Mr. Bader discussed slide 13: "Comparative Returns." He stated that the table illustrated the returns of the state's largest funds: PERS/TERS, CBR (Constitutional Budget Reserve) and the APFC (Alaska Permanent Fund Corporation.) He pointed out that the PERS and TRS and the Permanent Fund had similar earnings over time. Both funds outperformed the CBR. The purpose of the funds determined the investment strategy. He stated that the PER/TRS were invested for the long term. The permanent fund was a perpetual fund invested for the long term. The long term nature of the fund allowed the funds to invest in certain asset classes such as private equity called "ill-liquid" assets.

Mr. Bader discussed slide 14:

"ARMB Private Equity Program."

Private equity is largely made up of interests in limited partnerships that make equity investments in privately held operating companies.

Private equity is expected to deliver long-term returns in excess of the public markets and to enhance diversification. To earn higher returns, private equity gives up liquidity.

Performance has been good, generating 10.2% returns through 2013 versus a public market equivalent return of 4.6% for the S&P 500 and 5.1% for the Russell 3000.

The private equity program has generated \$800 million in additional fund value for the ARMB compared to investing in the public equity markets.

The ARMB started investing in private equity in 1998 and now has \$1.7 billion invested across 200+ partnerships; private equity is a 9% asset allocation for the ARMB.

Mr. Bader emphasized that prompt access to the CBR funds were necessary and therefore not conducive to investing in the long term asset class. The PER/TERS were expected to earn a higher percentage of return on investments after a transfer of funds from the CBR into the PERS/TRS Trust Fund.

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Commissioner Rodell turned to slide 16:

"Problem: \$11.9 Billion Retirement System Unfunded Liability."

The Public Employees Retirement System (PERS) and Teachers' Retirement System (TRS) combined unfunded liability is \$11.9 billion

- State Assistance payments to PERS and TRS rise from \$629 million in FY2014 to over \$1 billion per year

- Funding State Assistance solely through the operating budget crowds out funding for other vital public services
- Rating agencies express concern with the increasing liability

Commissioner Rodell moved to slide 17:

"Proposal: \$3 Billion Investment in Trust Funds."

Invest a total of \$3 billion in the Retirement Trusts in FY2015:

\$1.12 billion - Teachers' Retirement Fund

\$1.88 - Public Employees' Retirement Fund

Funding source: the Constitutional Budget Reserve

- Includes state assistance payments for FY2015.
- Beginning FY 2016, State Assistance payments would be fixed at \$500 million annually:

\$157 Million - PERS

\$343 Million - TRS

- State Assistance projected until FY2036; length of time depends on actuarial gains or losses experienced

Commissioner Rodell discussed the graph on slide 18: "Governor's Proposal." She noted that the graph depicted what the governor's proposal would look like over time. She pointed out that the previous graphs depicting level percent of pay (slide 9) and level dollar (slide 10) indicated variability in payment amounts from 2008 through 2014. The lump sum leveled out the annual payments to \$500 million per year.

Commissioner Rodell turned to slide 19:

"Governor Parnell's Approach.

- Pays down the retirement system debt rather than passing it on to future generations.
- A comprehensive and straight-forward approach addressing the problems of both PERS and TRS retirement systems.

- Addresses Alaska's biggest budget driver while keeping the State's promise to our retired public servants.
- Dramatically reduces future operating budget obligations and provides predictability for future budget planning.
- Improves municipal balance sheets and aligns the interest of the State of Alaska with our municipalities by sharing gains and losses.
- Addresses the number one credit concern raised by rating agencies.
- Improves and strengthens the health of the retirement systems.

Commissioner Rodell commented that the administration believed the legislation was the "right approach."

Commissioner Rodell provided a sectional analysis of HB 385. She read from the prepared sectional.

Section 1:

This section amends the Teachers' Retirement System (TRS) state assistance statute (AS 14.25.085). This statute was enacted in 2008 by SB 125, and currently provides that the state shall appropriate the amount sufficient to fully pay the total past service liability for the year at the employer contribution rate adopted by the Alaska Retirement Management Board (ARMB). In practice, this means that the State appropriates the amount that reflects the difference between the TRS employer contribution rate cap of 12.56% and the actuarial contribution rate to the TRS trust funds. In FY14, this amount was approximately \$317mm.

Section 1 amends AS 14.25.085 to implement the Governor's proposal. Under the Governor's proposal, \$1.1 billion would be appropriated from the constitutional budget reserve to the TRS trust fund, and then from FY16-FY36, an annual flat payment of \$343mm would be appropriated as state assistance.

The Governor's plan would convert the actuarial approach for TRS from an actuarial ratemaking paradigm to a fixed contribution paradigm. In a ratemaking paradigm, each year the actuary calculates what contribution rate is necessary to pay down the accumulated past service liability. In Alaska, this has resulted in highly volatile employer contribution rates that over the past decade have ranged from 12% to over 70%.

In a fixed contribution paradigm, the rate volatility is eliminated. Instead the annual contribution is fixed. In the case of TRS, the annual contribution is fixed at \$343mm. What can change each year, however, is the term of the amortization. Under the Governor's plan, the initial amortization term is 21 years—fixed payments of \$343mm through FY36. In the event of actuarial losses, the actuary may advise that the amortization term needs to be extended. So if there is a market downturn that results in investment losses in FY18, the actuary may advise that the amortization term must be extended to FY43 in order to fully amortize the TRS unfunded liability.

Co-Chair Stoltze referred to the payment language in the legislation that specified a fixed contribution "up to" \$343 million. He inquired how a fixed contribution could be any amount from \$0 to \$343 million.

Commissioner Rodell replied that the legislature retained its appropriation authority in the legislation. The administration recognized the legislature's right to determine the contribution amount. The governor intended to appropriate the fixed contribution amounts but included language in the legislation that payments were subject to legislative appropriation.

Commissioner Rodell continued with the sectional.

There could be cases where the actuarial loss over a particular period is sufficiently profound that payment of \$343mm over any length of amortization term is insufficient to fully pay off the unfunded liability. In such case, the actuary will assign a date on which the TRS trust fund will exhaust its funds unless the \$343mm annual payment amount is

increased. The actuaries call this date the "cross-over" point.

Co-Chair Stoltze wondered why the legislation did not use the term "at least" when referring to the contribution payment. He wanted the legislation to lend "moral guidance" to the legislature.

Commissioner Rodell replied that the goal of the language was to allow for legislative flexibility within the legislation.

Co-Chair Stoltze opined that both terms: "at least" and "up to" were not adequate. He felt that "up to" was ambiguous.

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Commissioner Rodell continued with the sectional and moved on to Section 2.

Section 2. This section implements the same amendment as does section 1, for the Public Employees' Retirement System (PERS) state assistance statute, AS 39.35.280.

A benefit to making this amendment in the PERS context is that a fixed contribution paradigm aligns the respective interests of all PERS employers. PERS employers all share in the actuarial gains, through having a shorter amortization schedule, and share in actuarial losses, through having a longer amortization schedule. Under the current version of AS 39.35.280, PERS municipal employers are largely indifferent to the impact of market downturns that create new unfunded liability because their rate does not change, and the State absorbs 100% of the impact of any new unfunded liability. The Governor's proposal cost shares such new unfunded liability in a fair way by extending the amortization term, so that PERS employers pay at the 22% capped contribution rate for a longer period of time.

Commissioner Rodell concluded with Section 3 and Section 4 of the sectional.

Section 3. This section makes the bill contingent on the enactment of constitutional budget reserve fund appropriations to TRS in the amount of \$1.1 billion, and to PERS in the amount of \$1.9 billion.

Section 4. Establishes the effective date of this act as July 1, 2014.

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DAVID TEAL, DIRECTOR, LEGISLATIVE FINANCE DIVISION, wanted to offer context to the figures in HB 385. He presented the fiscal outlook model [presented as an excel spreadsheet] (copy on file). He recapped that the model included the state's forecasted oil price and revenue and the operating budget which totaled \$4.35 billion. He pointed out that spending on the House budget was flat. The model comprised statewide operations, which included the debt service and the growing retirement contributions. Finally the model included a stagnant Capital budget of approximately \$550 million.

Mr. Teal reminded the committee that the budget was well beyond the long-term plan and the funding cap of \$5.6 billion announced by the governor. He relayed that the retirement plan was not included in the funding cap. He referred to a document that contained 2 graphs titled, "Unrestricted General Fund Revenue/Budget" (copy on file) and "Budget Reserves" (copy on file). He pointed out that the Budget Reserves bar graph depicted budget deficits escalating and the reserves depleted by 2024 in both the base scenario and current scenario. He remarked that the depleted reserves sparked the concern over retirement costs and cost containment. The bar graph demonstrated lower reserves over the next ten years in either plan. He said the "pay as you go" plan (base scenario) was designed to minimize near term costs. The plan improved the reserve position by \$2 billion which kept the reserves flexible to ensure cash for gasline investment. He offered that the governor's scenario, although accepted by the actuaries "cannot significantly improve" the near term health of the reserve fund. He concluded that the governor's plan was designed to improve the health of the retirement system in the long term and did not consider near term cash flow like the pay as you go plan, which reduced retirement contributions as much as possible.

Mr. Teal continued that the governor's plan which paid \$3 billion initially and \$500 million per year over the next 9 years totaled \$7.5 billion or half of the state's \$15 billion in reserves.

Mr. Teal discussed the long term outlook and examined the cumulative retirement costs. He turned to a graph titled "Cumulative Costs of Options to Eliminate TRS Unfunded Liability" (copy on file). The graph illustrated that the governor's plan, which extended into 2043 was initially \$1 billion higher than the base scenario paying lower yearly contributions. The total cost of the plan grew slower than the base scenario and crossed paths with the base scenario in 2023 similar to the previous graph. The results were the same; the early infusion of cash lowered annual payments and the lower annual payments eventually saved approximately \$.5 billion. He maintained that cheaper retirement costs lead to lower deficits in the future if the fiscal outlook remained the same.

Mr. Teal believed that the legislature faced tough choices in the future. The legislature must decide its level of commitment to maintaining a healthy retirement system and whether reserve flexibility was an issue. He declared that whether the reserves were used for a cash infusion into the retirement fund or for annual payments the retirement systems would "consume the same amount of reserves" in the 10-year period regardless of the payment option.

Mr. Teal discussed the graph, "Cumulative Costs of Options to Eliminate TRS Unfunded Liability". He pointed to the year 2025 at the approximately \$4.5 billion mark, where the lines intersect. He explained that reducing costs in the early years were linked to higher costs in total. High contributions in the early years brought lower costs in total. He deduced that the situation could be expressed as "you can pay now or you can pay more later." The relative position of the intersecting lines was maintained even when changing the payment variables for either plan. The costs met on the graph at approximately \$4.5 billion, which was the amount of the unfunded liability. He stated that "the bottom line" was paying more now significantly reduced total costs and paying lower payments now cost more in the "long run." All plans intersect at about 2025. He maintained that if the legislature was committed to a healthy retirement fund and knowing that using reserves for a cash infusion had no significant consequences for the

life or flexibility of the reserves why not choose the least expensive option in the long run.

Mr. Teal questioned why HB 385 contained the language "subject to appropriation" and "up to" when the actuarial recommended contribution could be higher than \$343 million at the standard amortization of 25 years. He concluded that if the legislature was seeking solutions that minimized contributions over the next ten years and took a long term view of the system then larger cash infusions were a better solution in the long run and in the short run. Minimizing contributions cost more but both approaches catch up to each other in the 2023 to 2025 year period. After that time "the deficits would be lower and the systems healthier."

Co-Chair Stoltze OPENED public testimony.

KAREN CRANE, ALASKA MUNICIPAL LEAGUE, spoke in strong support of HB 385. She relayed that the bill provided predictable and affordable annual payments for both the state and municipalities. The legislation kept the liability in check and allowed future earnings to offset future contribution requirements and strengthened the state and municipal credit ratings. The plan extended amortization of the unfunded liability and local government would "bear" a \$1.5 billion share of the liability. The league felt the time to deal with the issue was now and should not be left to burden future generation.

PAT BRANSON, MAYOR, KODIAK, testified in support of the legislation. She stated that the city supported the infusion of \$3 billion dollars into the PERS/TRS reserve account and maintaining the municipalities contribution rate of 22 percent. The provisions allowed for future interest in contribution requirements, reduced the budget pressure on state and local governments and facilitated planning for leaner budget years. She appreciated the committee's consideration.

LARRY DEVILBISS, MAYOR, MAT-SU BOROUGH, appreciated the legislation. The borough supported front-loading the liability. He stated that the municipalities contributed 22 percent to each payroll. The solution brought relief for tax payers by lifting the municipality's burden of the unfunded liability. He hoped for a solution that was fiscally responsible and fair to taxpayers.

BOB BARTHOLOMEW, FINANCE DIRECTOR, CITY AND BOROUGH OF JUNEAU, relayed the city's support for the governor's proposal. He understood that a contribution extension mandated by the actuary was a necessary expense. He challenged the notion that reducing the cost in the long term caused giving up flexibility or resources in the short term. He believed that transferring the lump sum money from the CBR into the retirement fund increased investment earnings. The potential returns were higher. He believed investment compounding was paramount. He felt that "compounded interest" was the "reward" of giving up short term reserve funds. The gain was a benefit to the initial loss of the reserve flexibility. The stabilization of the plan benefited both the state and local governments.

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MIM MCCONNELL, MAYOR, CITY OF SITKA (via teleconference), testified in support of HB 385. She stated the reason municipalities were in favor of the legislation. The bill enabled municipalities to plan a budget based on the 22 percent contribution rate which maintained necessary community services without increasing the local tax burden. She shared that the city increased its electric rates 49 percent since December 2012. The bill decreased the municipality's amount of the unfunded liability. She believed that addressing the liability now instead of sometime in the future was sensible.

JOHN SWEENEY, FINANCE DIRECTOR, CITY OF SITKA (via teleconference), stated that the city supported HB 385. He was grateful that the municipal contribution was maintained at 22 percent. The city of Sitka was currently deliberating its municipal budget. The legislation enabled proactive planning for municipal contributions to PRS/TRS funding. He cautioned that Sitka's budget process would become "reactive" if the legislation was not adopted. He urged for passage of the bill.

RICK KOCK, CITY MANAGER, KENAI (via teleconference), testified in support of the legislation. He appreciated the financial stability the legislation established for municipalities. He thanked the legislature for its diligent work on the issue.

JENNIFER JOHNSTON, ANCHORAGE ASSEMBLY, ALASKA MUNICIPAL LEAGUE, ANCHORAGE (via teleconference), testified in

support of the legislation. She noted that the unfunded liability for the city totaled \$651 million. She elaborated that new rules allowed that some or all of the money could be reallocated to either the city's enterprise fund or the water and waste water utility; Anchorage Water and Wastewater Utility (AWWU). She mentioned problems with the city's aging water treatment facilities and the costs associated with upgrades. She supported the process of front-loading the unfunded liability. She compared the unfunded liability to a how a credit card bill worked.

Co-Chair Austerman appreciated the fact that the city of Anchorage claimed its \$651 million share of the unfunded liability. He expressed frustration about the criticism the legislature received for allegedly not wanting to fulfill its retirement obligations. He appreciated the acknowledgement.

JIM WILLIAMS, CHIEF OF STAFF, CITY OF FAIRBANKS (via teleconference), supported the legislation. He commented that the bill was an "important and time sensitive opportunity" to control the projected unfunded liability and, by infusing cash into the system, eliminated an "uncertain" financial burden that would be transferred to municipalities. He discussed learning of a proposed 2 percent increase in the municipal PERS contribution rate. A two percent increase translated to a \$200 thousand budget expense for the City of Fairbanks, which could decrease services or increase property taxes. He appreciated the legislature's support.

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SALLIE STUVEK, HUMAN RESOURCES DIRECTOR, FAIRBANKS NORTH STAR BOROUGH (via teleconference), relayed the assemblies unified support for the legislation. She believed the \$3 billion cash infusion provided a sound financial model as a way of addressing and eliminating the unfunded liability by 2037. She stated that the cash infusion allowed municipalities to save in future contributions when state revenues would likely be reduced. The assembly passed a resolution (copy on file) in support of the cash transfer into the retirement trust fund in 2015. She appreciated the efforts to address the unfunded liability and maintaining the municipality's contribution rate of 22 percent.

JON BOLLING, CITY OF CRAIG (via teleconference), supported the legislation. He concurred with all of the previous testimony and expressed gratitude for the predictability maintaining the established 22 percent contribution rate provided.

STEPHANIE SCOTT, MAYOR, HAINES BOROUGH (via teleconference), testified in support of the legislation. She relayed that the assembly unanimously supported the \$3 billion cash infusion into the retirement fund. The assembly supported HB 385 and the premise that by "paying more now all will pay less later."

Co-Chair Stoltze noted that there had been a large volume of retirees interested in the bill. He favored the solution's approach, which was in the form of legislation rather than an appropriation. He stated that both bodies had been dealing with the retirement issues and expressed a commitment to making the deposits. He explained that the House Finance Committee's approach to separate out the Teachers' Retirement System (TRS) portion was well intended but not well received by the public. But there had always been an agreement about payment and that point was lost in the translation. He clarified that the current plan called for a \$3 billion withdraw from the Constitutional Budget Reserve "irrespective" of how it was apportioned and required a three-quarter vote from each house. The governor's legislation established certainty and "enshrined in statute" a guarantee with future politicians. The legislature would continue to discuss the issue with the governor's staff and with the Legislative Finance Division in an expedited fashion to pass the bill.

Co-Chair Austerman spoke about the unfunded liability and whose responsibility it was. He appreciated the municipalities' thanks for maintaining the 22 percent contribution rate but commented that he had not heard acknowledgement of the municipalities' liability which was approximately 42 percent. He stressed that the 22 percent paid by the municipalities left 20 percent of its liability unpaid. The remainder was shouldered by the state. By holding the contribution at 22 percent it meant there would be a longer payment period. If the legislature changed the municipalities contribution rate from 22 percent to 24 percent it would contribute to the upfront cost; however, the municipalities did not support the idea. He wished that the municipalities had voluntarily stepped forward to offer

to pay an additional 2 percent to lower the upfront costs. He pointed out that the liability was not just the state's responsibility. He emphasized that the state did not cause the liability. He remarked that a past "bad actuary" and the stock market crash caused the liability. He believed the responsibility of the unfunded liability should be shared and that while the state is paying the majority of the liability it is not exclusively the state's responsibility.

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Co-Chair Stoltze CLOSED public testimony.

HB 385 was HEARD and HELD in committee for further consideration.

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AT EASE

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RECONVENED

#sb104

CS FOR SENATE BILL NO. 104(FIN)

"An Act relating to appropriations from the dividend fund; creating the criminal fund; relating to appropriations from the criminal fund for payments for crime victims, operating costs of the Violent Crimes Compensation Board, grants for the operation of sexual assault response teams and domestic violence intervention projects, and incarceration costs; and providing for an effective date."

SENATOR FRED DYSON explained that in 1988 the legislature adopted restorative justice measures and enacted a criminal justice fund with the intention to restore victims to their pre-offense condition. He reported that the prior year's court ordered restitution totaled \$600 thousand for victims but only \$85 thousand was available to the Violent Crimes Compensation Board (VCCB) for distribution. He discovered that most of criminal's statutorily withheld Permanent Fund Dividend (PFD) was being diverted to cover prisoner's medical cost instead of funding victim's compensation. He expounded that SB 104 was a clean-up measure to clearly prioritize the distribution and use of the PFD criminal

fund to ensure adequate funding for victims compensation. He noted that his first attempt to structure the funds ensured that the victims received their money before court or other costs.

Senator Dyson clarified that the bill also allowed other victims support organizations to receive funding. He offered that the VCCB had advantages over other groups. The board appropriated funds to victims before the cases were adjudicated, which could take years. The victims were suffering and carried all of the costs. He added that the Department of Corrections (DOC) did not oppose the bill because of the increased payout of the dividends and that under the Affordable Care Act incarcerated criminals would be covered by Medicare and Medicaid. He added that the Department of Law (DOL) maintained a recovery section for court ordered funds that recently improved their recovery rates. Child support enforcement and collection by the Department of Revenue (DOR) would not be affected by SB 104.

Senator Dyson added that the bill received "rigorous" examination in the Senate and improved during the committee process.

Senator Dyson stated that the legislation would make an extraordinary difference for some of the victims. He added that the criminal fund did not relinquish the responsibility of the amount owed by the perpetrator. The criminal will reimburse the fund.

Representative Wilson asked whether the fund would pay all of the child support expenses owed by a criminal and wondered how the state would recover the costs.

JOSHUA BANKS, STAFF, SENATOR DYSON, answered that the Senate Finance version of the bill removed the child support arrears provision. He pointed out that on page 4, line 6 of the Senate Finance version the second priority distributed funds to the Council on Domestic Violence And Sexual Assault (CDVSA).

Senator Dyson interjected that he struggled with the child support issue. He worked with the administration and Child Support Services Division and a solution proved difficult. He delineated that child support arrears were exorbitant and would make a huge impact on the fund. Issues such as

how far back to assess arrears were problematic. The Senate Finance committee was unable to determine an equitable way to address child support issues. He acknowledged the need and thought a solution could be found in the future. Representative Wilson asked how the order of priorities was established.

Senator Dyson replied that the concept of restorative justice clearly intended that the first priority for the perpetrators restitution would be used to restore the victim to the pre-offense condition. He then examined the other entities that were entitled for court ordered reparations and pondered who the most worthy was. He concluded that organizations that provided services to victims were another high priority.

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Representative Holmes noted that the second priority appropriated funds to the CDVSA. She read page 4, lines 8 through 10:

... for grants for the operation of sexual assault response teams and domestic violence intervention projects that input data into the Alaska Public Safety Information Network...

Representative Holmes reported that the language in previous versions was broader. She wondered whether the change was substantive and if it would change the way funds were currently distributed to the program.

Mr. Banks replied that the language was established to focus on programs that were successful. The programs accomplished a large reduction in the rate of recidivism for domestic violence perpetrators and immediately responded to the victim's needs.

Representative Holmes restated that the provisions limited the flexibility of the funds use to two particular programs of CDVSA's broader mission.

Mr. Banks concurred.

Senator Dyson stated that setting priorities established a new source of funds to help victims and he advised that the legislature only distribute funds to organizations that

have a track record of providing services in an effective way.

Co-Chair Austerman asked what was meant by new funds.

Senator Dyson replied that the prior year's total criminal fund administered to DOC was \$13 million. He stated he misspoke. The funds were available for a new purpose.

Co-Chair Austerman asked what the cost of SB 104 was out of the \$13 million.

Mr. Banks referred to the chart regarding potential scenarios of the fund: "Historic PFD Criminal Fund Appropriations" (copy on file). He stated that the impact to the department for the next fiscal year was \$.5 million.

Co-Chair Austerman wanted clarification regarding the cost of the bill to the department and the \$8.4 million figure on the fiscal note FN7 (COR).

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Mr. Banks pointed to the first priority established on page 4 of the bill and noted that 20 percent of the criminal fund would be distributed to the VCCB. He clarified that based on the current years criminal fund of approximately \$10 million the total distributed to the board would be \$2 million. Currently DOC received \$1.5 million for victim's compensation. He noted that the projection for next year's PFD was \$1,300 to \$1,800. The criminal fund would significantly increase. He did not anticipate losses for the department if the later scenario occurred.

COMMISSIONER SCHMIDT, DEPARTMENT OF CORRECTIONS, explained that SB 104 re-prioritized the department's needs to meet the prisoners' medical needs. He exemplified the situation where a prisoner needed a lung transplant that cost \$800,000. The prisoner was medically paroled and treated at the Alaska Native Medical Center. If the prisoner had been denied treatment at the medical center, the law required that the department would have had to pay for the medical costs of the transplant. He relayed that the PFD funds

distributed to the department fluctuated each year. The department requested general fund money to backfill the anticipated need based on projections. If funds were lacking due to the legislation the department would request general fund money or make a supplemental request. He qualified that the department worked hard to control rising medical costs and made careful projections in order to avoid requesting supplemental funds.

Co-Chair Austerman asked what the prisoners' total medical budget was.

LESLIE HOUSTON, DEPUTY COMMISSIONER, DEPARTMENT OF CORRECTIONS, replied that the current year's total was \$41.268 million.

Commissioner Schmidt reiterated that DOC worked hard to achieve medical cost containment. He stated his neutrality about the bill but stressed that if the money fluctuated, the department would have no other choice except to request additional funding.

Co-Chair Stoltze addressed the \$8.4 million appropriation in DOC's fiscal note. He asked whether that was a worst case scenario projection in anticipation of decreased funding due to passage of the legislation.

Ms. Houston affirmed his assumptions.

Representative Holmes recalled much discussion about the spiraling cost of prisoner's medical care in DOC subcommittee. She remembered that prisoners were not eligible for any type of government assistance for medical care. She wondered how the Affordable Care Act would impact the department when prisoners qualified for medical care.

Commissioner Schmidt replied that coverage was limited. He continued that inmates' eligibility was complicated and that the department worked diligently with the Department of Health and Social Services (DHSS) to understand the process.

Ms. Houston reported that inmates that were 65 years of age and older, pregnant women, and unsentenced inmates would be covered under the Affordable Care Act. The unsentenced inmates were only covered outside of the correctional facility for a period of 24 hours in the hospital. She

expounded that Medicaid coverage was split 50 percent between the state and Federal government but that currently the split was 60 percent federal and 40 percent state when paying for hospital costs. The department did not yet know how much the department could leverage or recover under the Affordable Care Act coverage.

Representative Holmes asked whether someone who was covered under Medicaid or Medicare before they were incarcerated was still eligible when in prison under the Affordable Care Act.

Ms. Houston answered that once the person was adjudicated and sentenced they would not be eligible.

Representative Gara asked whether the felony classification disqualified the prisoner or just the fact that the person was incarcerated.

Ms. Houston read the four factors that disqualified the inmate: 1) convicted of a felony during the qualifying year; 2) incarcerated for a felony during the qualifying year; 3) convicted of or incarcerated for a felony during the qualifying year with two prior misdemeanor convictions that occurred after December 13, 1996; 4) convicted of or incarcerated for a misdemeanor during the qualifying year with a prior felony conviction.

Representative Munoz asked about the possibility of enrolling higher costs prisoners in the program and paying the premiums.

Ms. Houston stated that inmates were not eligible for the general Affordable Health Care coverage.

Representative Costello mentioned the \$42 million cost of inmates' health care and asked what the amount spent on prescription drugs was.

Ms. Houston answered that she would supply the data after the meeting.

Representative Wilson asked whether the four disqualifiers for Affordable Care Act coverage were prohibited by state or federal law. She wondered whether inmates that were covered by private insurance were prohibited coverage by state or federal law.

Ms. Houston answered that the prohibitions were from the code of federal regulations.

Co-Chair Stoltze requested clarification on how the role of the PFD Division interacted with the criminal fund and how the legislation affected the division.

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DAN DEBARTOLO, DIRECTOR, PFD DIVISION, DEPARTMENT OF REVENUE, replied that the bill did not change the calculation of the criminal fund and was the reason the division submitted a zero fiscal note. He pointed to page 2, line 12 of CS SB 104 FIN which delineated the three categories of individuals who were counted in the criminal calculation. He read:

(A) during the qualifying year, the individual was convicted of a felony;(B) during all or part of the qualifying year, the individual was incarcerated as a result of the conviction of a(i) felony; or(ii) misdemeanor if the individual has been convicted of a prior felony or two or more prior misdemeanors.

Mr. Debartolo furthered that each year DOC and the Department of Public Safety (DPS) sent the division the list of the individuals who met the criteria. The division matched them against individuals who applied for the dividend. The amount of applicants who applied for the dividend was smaller since many categorized individuals realized they were ineligible for a PFD. The division then ascertained who would be otherwise eligible if they did not fall into the three categories which typically amounted to 95 percent. The applicants and non-applicant offenders were added together to yield a count which was multiplied by the dividend amount. The total amount was the criminal fund and sent to the Office of Management and Budget (OMB) for distribution. He added that the amount fluctuated greatly since 2008 and for the current fiscal year was \$9.6 million. He informed the committee that the division did not decide how the fund was distributed but merely calculated the amount.

Co-Chair Austerman asked how much of the \$9.6 million was distributed to DOC.

Mr. Houston reported that the department received \$10,000,474 in FY14 in criminal receipts.

Mr. DeBartolo replied that he attributed the \$9.6 million calculation was to FY 15.

Ms. Houston replied that the department anticipated \$8,445,900 in criminal receipts as requested in the fiscal note.

CSSB 104(FIN) was HEARD and HELD in committee for further consideration.

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ADJOURNMENT

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The meeting was adjourned at 5:11 p.m.