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**PERS/TRS:
OVERVIEW
&
UPDATE**

SFIN

FILE

Sen. G.
Stevens
Rep. Hawker



Department of Administration

Financial Overview
PERS and TRS

Senate Finance

February 2, 2007

Department of Administration
PERS and TRS
Financial Overview



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Department of Administration
PERS and TRS
Financial Over



SB 141 Established the Alaska Retirement Management Board (ARMB). AS 37.10.210 states, "The board has the fiduciary obligation to manage and invest these assets in a manner that is sufficient to meet the liabilities and pension obligations of the retirement systems."

SB 141 also provided for Important Protections under AS 37.10.220

- Conduct experience analysis not less than once every four years
- Healthcare assumptions shall be reviewed annually
- Actuarial assumptions shall be reviewed and certified by a second actuary
- Independent Audit of actuary conducted not less than once every four years
- Independent audit of performance consultant not less than once every four years



Actuarial Valuation Results

In November 2005 Buck Consultants was awarded contract to provide professional actuarial services to the Division of Retirement and Benefits.

In March of 2006 Buck performed a replication and actuarial review of methods and assumptions used by Mercer in the June 30, 2004, valuations. Correction of errors discovered in the replication process were incorporated into the June 30, 2005, valuation reports for PERS and TRS. Principal replication findings are summarized as follows:

- Did not find significant errors or concerns regarding *pension* liabilities for PERS or TRS.
- Found several items in replication process where Mercer failed to properly value medical liabilities for PERS. This resulted in approximately \$399 million understatement for PERS medical liabilities.

Based on the valuation results, the increase to the employer contribution rates for FY08 compared to FY07 are as follows:

| | <u>FY07</u> | <u>FY08</u> |
|------|-------------|-------------|
| PERS | 28.19% | 32.51% |
| TRS | 41.78% | 42.26 |



Level Dollar Amortization Schedule

At the request of the ARMB, Buck Consultants calculated FY08 rates based on a level dollar amortization of the unfunded liability for the PERS and TRS. The current funding policy adopted in 2002 amortizes the initial unfunded liability and the change in the unfunded liability in subsequent years over a fixed 25-year period, using a 4.25% payroll growth assumption.

The plan is now closed to new members so it is appropriate to not use a 4.25% payroll growth assumption. The ARMB adopted the rates developed using the level dollar amortization method.

Two important points:

- Closing the defined benefit plans to new members does not increase the unfunded liability to the plans
- Adopting the level dollar amortization schedule does not increase the unfunded liability to the plans

What does not using the payroll growth factor do?

- Removing the payroll growth factor acts to increase the contribution rates for FY08. However, according to Buck it will result in a lower contribution schedule in future years.

| | <u>FY07</u> | 2005 Valuation <u>FY08</u> | Level Dollar Amortization <u>FY08</u> |
|------|-------------|----------------------------------|---|
| PERS | 28.19% | 32.51% | 39.76% |
| TRS | 41.78% | 42.26% | 54.03% |



Actuarial Experience Analysis

Buck Consultants completed the actuarial experience analysis in October 2006. Purpose of actuarial experience study is to compare actual plan experience with actuarial assumptions used in the valuation. The experience study looked at the five year period from 2001 through 2005.

- (1) Actuary will recommend changes to assumptions if sufficient data is available that shows material difference between expected and actual experience.
- (2) Future experience is likely to be different given recent trends.

Several of the assumptions include: investment return, healthcare, mortality, retirement, salary, Alaska residency, actuarial cost method, and disability.

To get an understanding of the impact of the revised assumptions and actuarial methods, Buck recalculated FY08 rates using the revised assumptions and actuarial methods. The results are summarized below.

| | 2005 Valuation <u>FY08</u> | Level Dollar Amortization <u>FY08</u> | Actuarial Experience Study <u>FY08</u> |
|------|----------------------------------|---|--|
| PERS | 32.51% | 39.76% | 46.64% |
| TRS | 42.26% | 54.03% | 59.56% |

The ARMB adopted the recommendations by Buck, which had been reviewed by GRS (second actuary) and determined to be reasonable. The revised assumptions and actuarial methods will be incorporated into the June 30, 2006, actuarial valuation reports.

Alaska Public Employees' and Teachers' Retirement Systems Earnings – Actuarial Rate – Employer Rates – Funding Ratios

Public Employees' Retirement System

| Valuation Year | FY 01 | FY 02 | FY 03 | FY 04 | FY 05 |
|---|--------------|--------------|--------------|--------------|--------------|
| Employer Contribution Fiscal Year | <u>FY 04</u> | <u>FY 05</u> | <u>FY 06</u> | <u>FY 07</u> | <u>FY 08</u> |
| Actual Investment Return | (5.25%) | (5.48%) | 3.67% | 15.08% | 8.95% |
| <u>Actuarial</u> Investment Return | 8.25% | 8.25% | 8.25% | 8.25% | 8.25% |
| Unfunded Liability, <u>in billions</u> | \$0.73 | (\$2.4) | (\$2.9) | (\$3.4) | (\$4.4) |
| Average Calculated Rate | 6.77% | 24.91% | 25.63% | 28.19% | 32.51% |
| Board Adopted Rate | 6.77% | 11.77% | 16.77% | 21.77% | *39.76% |
| Funding Ratio – Assets \ Liabilities | | | | | |
| Total Benefits | 100.9% | 75.2% | 72.8% | 70.2% | 65.7% |
| Total Employer Contribution Amount In Millions | \$105.6 | \$178.2 | \$272.3 | \$354.8 | \$676.8 |

Teachers' Retirement System

| Valuation Year | FY 01 | FY 02 | FY 03 | FY 04 | FY 05 |
|---|----------------|----------------|----------------|----------------|----------------|
| Employer Contribution Fiscal Year | <u>FY 04</u> | <u>FY 05</u> | <u>FY 06</u> | <u>FY 07</u> | <u>FY 08</u> |
| Actual Investment Return | (5.35%) | (5.49%) | 3.68% | 15.09% | 9.01% |
| <u>Actuarial</u> Investment Return | 8.25% | 8.25% | 8.25% | 8.25% | 8.25% |
| Unfunded Liability, <u>in billions</u> | (\$0.2) | (\$1.7) | (\$2.1) | (\$2.3) | (\$2.5) |
| Average Calculated Rate | 14.44% | 35.57% | 38.85% | 41.78% | 42.26% |
| Board Adopted Rate | 12.00% | 16.00% | 21.00% | 26.00% | *54.03% |
| Funding Ratio – Assets \ Liabilities | | | | | |
| Total Benefits | 95.0% | 68.2% | 64.3% | 62.8% | 60.9% |
| Total Employer Contribution Amount In Millions | \$68.7 | \$93.5 | \$128.0 | \$164.3 | \$351.7 |
| Total PERS/TRS Unfunded Liability | \$0.053 | (\$4.4) | (\$5.0) | (\$5.7) | (\$6.9) |

On Oct 4, 2006, the ARMB was presented with the results of the Actuarial Experience Analysis by Buck Consultants that recommended adjustments to the assumptions for PERS and TRS. The ARMB adopted Buck's recommendations. The recommended adjustments will be incorporated into the FY06 valuations that will set the FY09 employer rates for PERS and TRS. Using the FY05 valuations, Buck Consultants has estimated the adjustments to the assumptions will increase the unfunded liability to approximately \$8.6 billion (\$5.5 PERS and \$3.1 TRS).

* Level dollar amortization schedule adopted by the ARMB.

October, 2006
Division of
Retirement and
Benefits