

3/14/07

PERS

DEFINED

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FILE

Public Employees' Retirement System (PERS)

Defined Benefit (DB) Plan

Accounting Issues

Senate Finance
March 14, 2007

Division of Retirement and Benefits
PO Box 110203
Juneau, AK 99811-0203
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Why are we here today?

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





Proposed Solution

- Cost share legislation
 - Administer the PERS DB plan like the TRS DB plan
 - State to assume 65% of unfunded liability at 6/30/2006 (estimated \$3.6B of \$5.5B total)
 - All employers share the cost (benefits, administration and investment)
 - Simplify administration



Proposed Solution (cont.)

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

PERS = One System but Two Plans



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



PERS DB

Accounting Issues

No impact on:

- Teachers' Retirement System (TRS)
- Benefits paid to members
- PERS DB Plan level accounting (PERS as a whole)
- New PERS Defined Contribution Retirement Plan (Tier IV)



Agent Multiple Employer Plan

Defined and described as follows:

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



Alaska Statutes

AS 39.35.100 (b) (3)

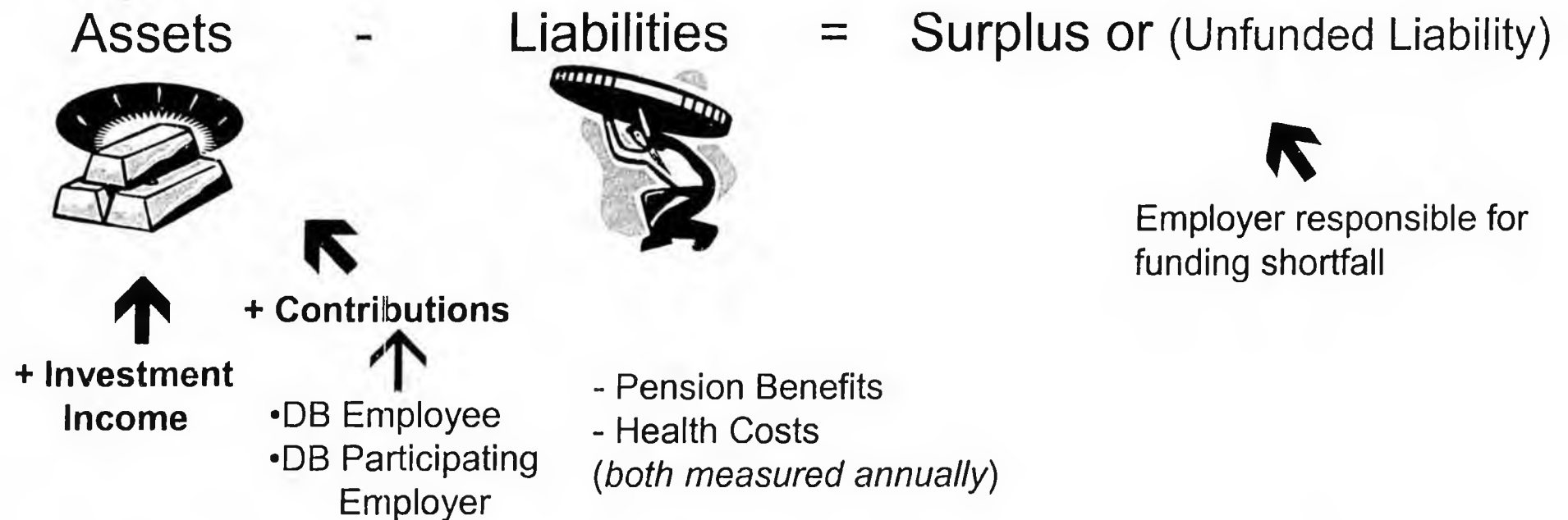
- A separate account for each employer shall be maintained.
- The account shall be credited with contributions of the employer.
- This account shall be charged with the employer's actuarial charge for pension, death benefits, and other benefits paid under this plan to or on behalf of the employee of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

Alaska Statutes (cont'd)

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



PERS DB Plan



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



9:46:12

Assets

Employer contributions are accounted for in two separate buckets:

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





Retiree Reserve Account

Funding Sources

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



Transfers

- In order to calculate an employer's past service contribution rate, we assign retiree reserve assets to employers
- Allocation process is used to assign retiree reserve assets to individual employers



Allocation Process

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

Allocation example

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

	<u>Assets</u>	<u>Liabilities</u>
Active	\$237,819	350,172
Allocated share of retiree reserve account	-	-
Total	<u>\$237,819</u>	<u>350,172</u>

- Unfunded liability is \$112,353
- Employer has no retirees at 6/30/2004, so has not contributed to the retiree reserve account





Next year – FY05

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



The allocation

Employer retiree liabilities	\$	453,428
Total retiree liabilities		<u>7,131,974,579</u>
% allocated to employer		.006%
Retiree reserve account balance		<u>6,194,055,956</u>
Account balance allocated to employer	\$	393,883

Even though employer has not contributed to this account

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



Transfer

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

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

The transfer

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

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



Effect of allocation and transfer

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

	<u>Assets</u>	<u>Liabilities</u>
Active (237,819 + 32,261-59,545)	\$ 210,535	18,107
Allocated share of retiree reserve account (393,883 + 59,545)	<u>453,428</u>	<u>453,428</u>
Total	\$ 663,963	471,535

■ Over funded by \$192,428.





Liabilities

- Annually calculated by employee
 - Allocated to individual employer
 - Based on pro rata service earned with employer
 - Does not take into account salary earned with employer
 - Concerns have been raised about this allocation process as well



Liability allocation example

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

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

Example (cont.)

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

	<u>Salary Paid</u>	<u>Service Earned</u>	<u>% by employee</u>	<u>Liability Allocated</u>
City X	\$ 1,000	5 yrs	50%	\$375,000
City Z	\$ 200,000	<u>5 yrs</u>	<u>50%</u>	<u>375,000</u>
Total		10 yrs	100%	\$750,000

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

Impact on Contribution Rates

Assets - Liabilities = Surplus or
(Unfunded Liability)



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

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



Proposed Solution

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



1.3.12.12



ALASKA STATE LEGISLATURE

SENATE FINANCE COMMITTEE

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MEMORANDUM

DATE: March 14th, 2007

TO: Senate Finance Committee Members and Staff

FROM: Senator Bert Stedman, Co-Chair

RE: February 20th PERS & TRS Presentation Follow-up

On February 20th, David Teal, Legislative Finance Division Director gave the committee a brief overview of the financial assistance the state has provided to PERS employers over the last 4 years.

During the presentation, a question was raised about what impact a large cash infusion might have on employer contribution rates. Last fall, the Division of Retirement and Benefits asked Buck Consultants, the state's actuary, to calculate the impact of a single \$500 million cash contribution on future employer contribution rates for PERS and TRS. Buck provided that information to the Division on October 9th, 2006 and I've attached it for your information.

Mr. Teal's presentation also included bar charts showing state and local contributions to PERS from FY 2004 to FY 2008 as a percentage (page 6) and in dollars (page 7). The charts only showed what actual contributions were made - not what contributions the state's actuaries recommended should be made. Because the actuarially calculated contribution rates were much higher than those actually adopted by the Alaska Retirement Management Board (ARMB) and its predecessor boards, I had those charts redone to show that difference. The new charts are attached for your information.

I look forward to continuing to work with you on this important issue over the next several months.

Attachments:

- 1) Letter to Ms. Traci Carpenter, Dir, Div of Retirement and Benefits from David H. Slisinsky, Principal and Consulting Actuary, Buck Consultants dtd 10/9/06 (3 pgs)
- 2) Excel charts - State & Local Contributions to Local PERS by % and by \$ (2 pgs)

cc:

David Teal, Director, Leg Fin Div
Melanie Milinorn, Director, R&B, Dept of Admin
Senate Finance Committee Secretary

October 9, 2006

VIA EMAIL

Ms. Traci Carpenter
Director
State of Alaska
Department of Administration
Division of Retirement and Benefits
333 Willoughby Avenue
6th Floor State Office Building
Juneau, AK 99811-0208

Re: PERS and TRS – Effect of Additional \$500 Million State Contribution

Dear Traci:

As requested, we have set up three different scenarios to calculate the impact of a \$500 million contribution on the future Employer Contribution Rates for the State of Alaska Public Employees' Retirement System (PERS) and Teachers' Retirement System (TRS). The three scenarios that were taken into consideration were:

- Scenario 1: 100% of the contribution allocated to TRS,
- Scenario 2: 100% of the contribution allocated to PERS, and
- Scenario 3: Allocate \$500 million based on the unfunded liability of PERS and TRS as of June 30, 2005.
This allocation provides for a \$182.9 million contribution to TRS and \$317.1 million to PERS.

The scenarios were calculated as of the most recent actuarial valuation as of June 30, 2005. The contribution is assumed to be made on January 1, 2007. The results of our calculations are attached.

Exhibit 1 shows a 25-year projection of expected employer contribution rates based on DB payroll only. Exhibit 2 shows the expected amount of employer contributions during the same period, and the savings to employer contributions over 25 years resulting from the additional contribution.

The results are based on the data, assumptions, methods and plan provisions as described in the June 30, 2005 valuation reports. The amortization of the past service cost rate assumes no payroll growth. All other assumptions are the same as the valuation.

If you have any questions regarding these calculations, please call.

Sincerely,



David H. Slushinsky, ASA
Principal and Consulting Actuary

/mlp

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Enclosures

c: Ms. Charlene Morrison
Ms. Michelle DeLange

**State of Alaska PERS and TRS
Projected Impact of Additional Funding
Projection of Actuarial Contribution Rates on DB Payroll Only**

PERS				TRS			
Fiscal Year	Current Projections	Scenario 2	Scenario 3	Fiscal Year	Current Projections	Scenario 1	Scenario 3
2006	16.77%	16.77%	16.77%	2006	21.00%	21.00%	21.00%
2007	21.77%	21.77%	21.77%	2007	26.00%	26.00%	26.00%
2008	39.76%	39.76%	39.76%	2008	54.03%	54.03%	54.03%
2009	41.68%	41.68%	41.68%	2009	53.14%	53.14%	53.14%
2010	46.35%	43.38%	44.47%	2010	60.01%	51.43%	56.87%
2011	48.47%	45.06%	46.31%	2011	62.17%	52.44%	58.61%
2012	51.13%	47.22%	48.65%	2012	66.20%	55.02%	62.11%
2013	53.52%	49.33%	50.87%	2013	70.80%	58.70%	66.37%
2014	56.21%	51.71%	53.36%	2014	75.95%	62.92%	71.18%
2015	59.40%	54.60%	56.36%	2015	80.68%	66.82%	75.61%
2016	61.99%	56.89%	58.76%	2016	86.05%	71.14%	80.60%
2017	65.52%	60.05%	62.05%	2017	93.76%	77.34%	87.76%
2018	69.07%	63.19%	65.34%	2018	105.28%	86.94%	98.57%
2019	73.18%	66.77%	69.11%	2019	112.26%	92.56%	105.05%
2020	80.28%	73.15%	75.76%	2020	123.56%	101.79%	115.59%
2021	86.02%	78.25%	81.09%	2021	135.15%	110.94%	126.29%
2022	92.71%	84.18%	87.29%	2022	160.68%	131.95%	150.17%
2023	99.82%	90.38%	93.83%	2023	177.76%	145.68%	166.02%
2024	112.37%	101.49%	105.46%	2024	205.31%	168.28%	191.77%
2025	128.86%	116.25%	120.86%	2025	231.28%	189.57%	216.02%
2026	141.00%	127.02%	132.12%	2026	258.19%	211.38%	241.06%
2027	156.53%	140.76%	146.52%	2027	299.28%	244.25%	279.14%
2028	174.58%	156.61%	163.17%	2028	389.64%	318.05%	363.45%
2029	209.01%	187.19%	195.16%	2029	467.07%	381.38%	435.72%
2030	161.35%	135.26%	144.79%	2030	328.54%	230.35%	292.62%
2031	172.32%	142.00%	153.07%	2031	379.36%	245.33%	330.33%

Scenario 1: Add to TRS an additional \$500 million in FY07

Scenario 2: Add to PERS an additional \$500 million in FY07

Scenario 3: Allocate \$500 million based on the unfunded liability in FY07 (\$182.9 million for TRS and \$317.1 million for PERS)

Data, Assumptions, Methods and Plan Provisions:

- Assets are assumed to earn 8.25%.
- The additional contribution is assumed to be made on January 1, 2007. Therefore, the first rate that will be impacted is for FY10.
- Assumes contribution will be on DB payroll only.
- No payroll growth is used for FY08 rates and later.
- No new members after July 1, 2006.
- All other data, assumptions, methods and plan provisions are the same as those described in the June 30, 2005 valuation reports

**State of Alaska PERS and TRS
Projected Impact of Additional Funding
Projection of Actuarial Contribution**

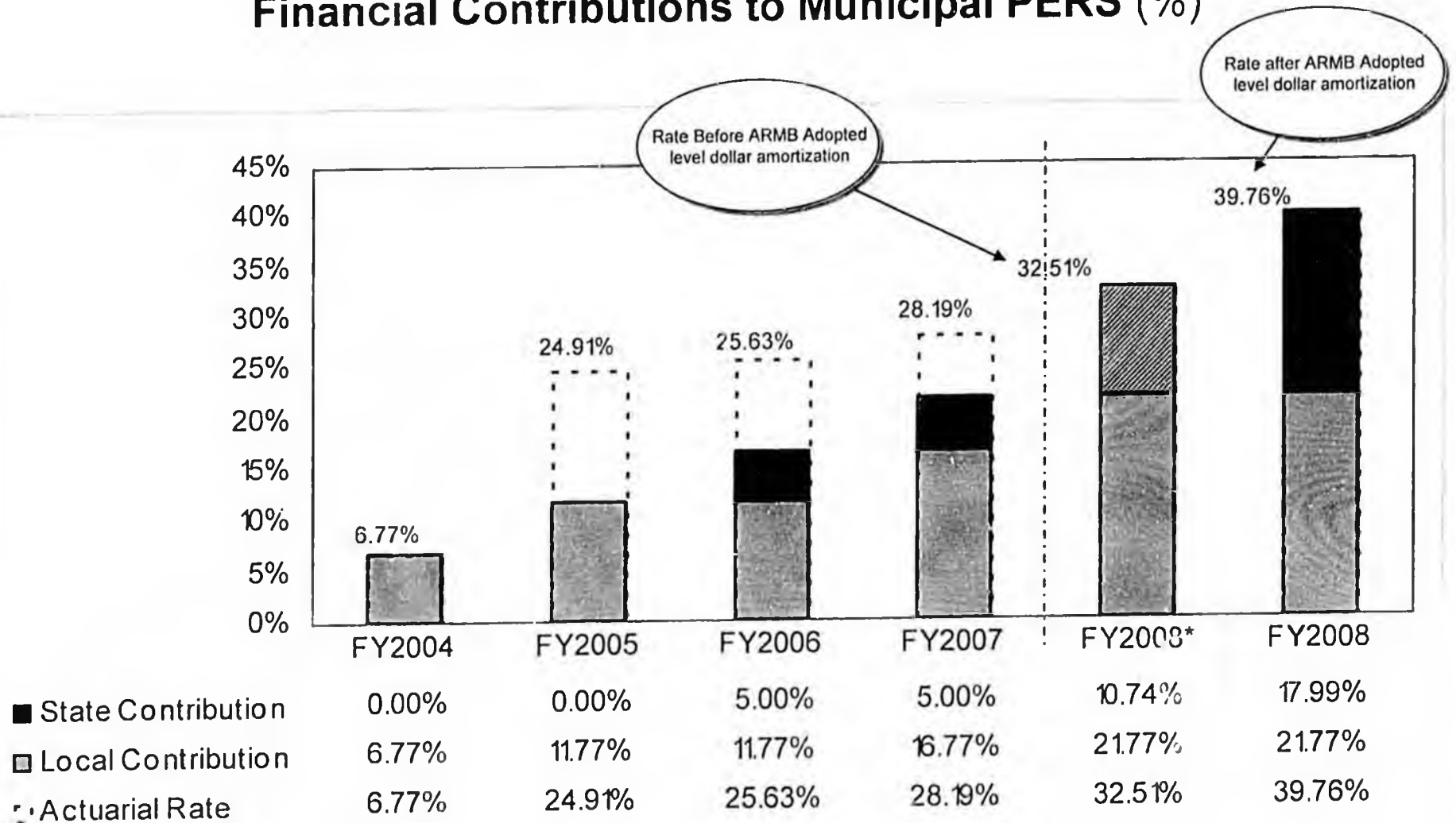
PERS				TRS			
Fiscal Year	Current Projections	Scenario 2	Scenario 3	Fiscal Year	Current Projections	Scenario 1	Scenario 3
2006	\$ 266,122	\$ 266,122	\$ 266,122	2006	\$ 117,764	\$ 117,764	\$ 117,764
2007	356,010	856,010	673,110	2007	148,886	648,886	331,786
2008	615,097	615,097	615,097	2008	289,826	289,826	289,826
2009	616,035	616,035	616,035	2009	275,138	275,138	275,138
2010	654,751	612,796	628,194	2010	296,199	253,849	280,700
2011	654,781	608,715	625,601	2011	290,951	245,415	274,290
2012	657,480	607,201	625,589	2012	293,955	244,311	275,794
2013	655,046	603,763	622,612	2013	300,369	249,035	281,575
2014	657,057	604,455	623,743	2014	304,028	251,869	284,934
2015	656,760	603,688	623,148	2015	297,698	246,556	278,990
2016	647,179	593,935	613,458	2016	289,435	239,284	271,104
2017	637,911	584,654	604,126	2017	299,844	247,333	280,656
2018	614,819	562,479	581,617	2018	310,515	256,423	290,724
2019	609,087	555,736	575,212	2019	303,087	249,900	283,621
2020	621,086	565,925	586,117	2020	286,941	236,385	268,432
2021	612,816	557,462	577,694	2021	288,449	236,778	269,539
2022	584,316	530,555	550,156	2022	304,787	250,291	284,851
2023	556,002	503,421	522,638	2023	306,657	251,315	286,404
2024	579,061	522,994	543,452	2024	323,530	265,177	302,193
2025	603,189	544,162	565,741	2025	317,122	259,931	296,198
2026	591,726	533,057	554,460	2026	279,220	228,597	260,694
2027	554,086	498,264	518,653	2027	280,003	228,518	261,161
2028	532,062	477,296	497,288	2028	329,784	269,191	307,617
2029	565,899	506,821	528,400	2029	297,883	243,233	277,889
2030	390,286	327,178	350,230	2030	166,281	116,585	148,101
2031	362,420	298,652	321,934	2031	158,755	102,666	138,236
Total	\$ 14,851,084	\$ 14,156,471	\$ 14,410,426	Total	\$ 7,157,106	\$ 6,504,256	\$ 6,918,219
Savings		\$ 694,613	\$ 440,658	Savings		\$ 652,850	\$ 238,887

- Scenario 1: Add to TRS an additional \$500 million in FY07
- Scenario 2: Add to PERS an additional \$500 million in FY07
- Scenario 3: Allocate \$500 million based on the unfunded liability in FY07 (\$182.9 million for TRS and \$317.1 million for PERS)

Data, Assumptions, Methods and Plan Provisions:

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- No additional contribution is assumed to be made on January 1, 2007. Therefore, the first rate that will be impacted is for FY10.
- Assumes contribution will be on DB payroll only.
- No payroll growth is used for FY08 rates and later.
- No new members after July 1, 2006.
- All other data, assumptions, methods and plan provisions are the same as those described in the June 30, 2005 valuation reports.

Financial Contributions to Municipal PERS (%)



Financial Contributions to Municipal PERS (\$ Mill)

