SCOMM

142.10

NRTA
AARP's Educator Community

TRADITIONAL DEFINED BENEFIT PENSION PLANS:

A Tried and True System That Benefits Taxpayers

The traditional public pension system is the best way to ensure taxpayers can reliably receive vital services. It's a cost-effective, proven and stable method to attract and retain qualified people to perform critical public sector work.

Dismantling and replacing the traditional pension system with new private accounts will result in higher costs for taxpayers and bureaucratic chaos.

The traditional pension system works - and has for more than 100 years. It is flexible and provides vital services to taxpayers at a low cost. Further, it provides a modest and stable retirement income for workers who have dedicated their career to serving the public.

FACTS ABOUT PUBLIC PENSIONS

The public pension system safeguards the delivery of vital taxpayer services.

Taxpayers will pay MORE to move to millions of private accounts.

The traditional public pension system is sound.

Funding shortfalls can be avoided.

The traditional public pension system is a vital stimulus to the economy.

States that have attempted a radical reform of public pensions have failed.

Taxpayers will foot the bill for workers who outlive inadequate, unstable retirement income.

The Disadvantages of Replacing Defined Benefit Plans with Defined Contribution Plans for State and Local Governments, Their Employees and Taxpayers

Legislation has been proposed in several states to replace state and local government defined benefit (DB) retirement plans with 401(k)-type retirement accounts called defined contribution (DC) plans. The issue is not whether state and local employees should have access to DC plans – most already do in conjunction with their DB plans or else through DC-type plans,[1] which play a useful role in providing supplemental, tax-deferred retirement savings. Rather the question is whether defined benefit plans should be eliminated and replaced with defined contribution plans.

While recognizing defined contribution plans are useful in providing supplemental retirement benefits, there are distinct advantages of maintaining state and local DB plans and disadvantages against replacing them with DC plans. Eliminating a DB plan and switching to a DC plan is a lose-lose situation for governments, their employees, and taxpayers for the reasons listed below.

1. Switching to a DC plan will cost state and local governments more over the short-term. Long-term cost savings are uncertain at best.

2. Almost all state and local DB plans provide disability and survivor benefits as well as retirement income. Switching to a DC plan would require employers to obtain these benefits from another source, and at a higher cost.

3. DB plans enhance the ability of state and local governments to attract qualified employees and retain them throughout their careers. Switching to a DC plan would limit this ability, possibly producing or exacerbating labor shortages in key service areas by increasing employee turnover rates. Higher turnover rates result in increased training costs and lower levels of productivity that can, in turn, result in the need for a larger total workforce.

4. DB plans help state and local governments manage their labor force by providing flexible incentives that encourage employees to work longer or retire earlier, depending on the circumstances. Switching to a DC plan would limit this flexibility and make these incentives more expensive for the employer.

5. DB plans lower overall retirement benefit costs by pooling the risks of outliving retirement benefits and of investment losses over a relatively large number of participants. Switching to a DC plan would require each individual to bear these risks alone, consequently requiring higher contributions than if the risks were pooled.

---

[1] Examples of DC-type plans available to state and local employees include 457 governmental deferred compensation plans and 403(b) annuities. In addition, some state and local employees are also covered by 401(k) plans, if the plans were established before May 6, 1986. According to testimony by the National Association of Government Defined Contribution Administrators before the U.S. House Ways and Means Oversight Subcommittee on March 23, 1999, 48 states and over 5,000 local governments have 457 plans, through which an estimated 8 million employees save for retirement. This is over 40 percent of the nation's state and local government employees.

6. DB plans earn higher investment returns and pay lower investment management fees than DC plans. Switching to a DC plan is likely to lower investment earnings used to finance retirement benefits and increase management costs, to the detriment of plan members.

7. DB plan investment earnings reduce future employer contributions. Switching to a DC plan would prevent state and local governments from reducing employer contributions through investment earnings, which currently fund over two-thirds of public retirement benefits.

8. DB plans provide secure retirement benefits based on a person's salary and period of service. Switching to a DC plan result in lower and less secure retirement benefits for many long-term governmental employees, including teachers, police officers, and firefighters, who constitute over half of state and local government workers.[2] State and local employees who are without Social Security coverage would be put at even greater risk.

9. DB plans help sustain state and local economies by providing adequate retirement benefits for a significant portion of the workforce. Switching to a DC plan may slow state and local economies, since a large number of retirees would likely receive lower retirement benefits.

10. Switching to a DC plan is likely to result in pressure on state and local governments to increase DC plan benefits and provide additional financial assistance for public sector retirees.

---

[2] U.S. Department of Commerce, U.S. Census Bureau, *Statistical Abstract of the United States 2004-2005* (Washington, DC: U.S. Government Printing Office, 2004), Table No. 454. Teachers, school employees, police officers, and firefighters constitute approximately 60 percent of state and local government employees.

BACKGROUND

State and local government retirement plans in the United States cover 14 million active employees (about 10 percent of the U.S. labor force) and 6 million retirees,[3] including teachers, police officers, firefighters, legislators, judges, and general employees. In 2003, state and local retirement plans had over $2 trillion in assets and paid annual benefits of $122 billion, averaging about $18,500 per retiree.[4] Ninety percent of state and local governmental employees are covered by defined benefit retirement plans.[5] Approximately 25 percent are not covered by Social Security, including close to half of public school teachers and three-quarters of police officers and firefighters.[6]

Since the mid-1990s, legislation has been proposed in several states to replace state and local DB plans with DC plans. Over the last two years, the pace of these proposals has increased, due to downturns in the investment markets and resulting higher contribution rates for many DB plans. Proponents of the change argue that switching to a DC plan would lower the government's cost of providing retirement benefits, thereby reducing state and local taxes. They also argue that DC plans would benefit public employees by giving them higher benefits through DC plan investment earnings and by making it easier for employees to take their benefits with them when they change jobs.

As this paper shows, it is likely that switching to a DC plan would increase a government's retirement costs over the short-term, and possibly over the long-term as well. In addition, recent studies indicate that retirement benefits provided though DC plans are, on average, significantly lower than those provided through DB plans. Moreover, while DC plans are useful for providing supplemental, tax-deferred retirement savings, replacing DB plans with DC plans could cause severe, unintended consequences:

- Governments could lose a valuable tool for attracting and retaining qualified employees;
- Public employees could lose a significant amount of retirement income, potentially affecting state and local economies; and
- Legislators could face additional pressure to increase DC retirement benefits and provide additional financial assistance for public sector retirees.

---

[3] U.S. Department of Commerce, U.S. Census Bureau, *2003 State and Local Government Public Employee Retirement System Survey*, Table 5.

[4] Ibid. Table 1. Average benefit calculated by the author and rounded to the nearest thousand dollars.

[5] U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits in State and Local Governments, 1998* (Washington, DC: U.S. Government Printing Office, 2000), p. 5.

[6] Keith Brainard, *Public Fund Survey, Summary of Findings, FY 2003*, September 2004. The Public Fund Survey is sponsored by the National Association of State Retirement Administrators (NASRA) and the National Council on Teacher Retirement (NCTR). Respondents represent over 80 percent of U.S. state and local retirement system assets and covered membership.

HOW DEFINED BENEFIT PLANS WORK

In a typical DB plan, employers promise to pay retirement benefits based on an employee's period of service and final average salary. A typical benefit formula for state and local general employees is 2 percent times final average salary times years of service.[7] Under this formula, an employee who works 20 years and retires with a final average salary of $40,000 would earn an annual benefit of $16,000.

Eligibility for the benefit (i.e., vesting) usually requires employees to work for a minimum period of time, typically 5 years.[8] Upon retirement, the benefit is provided as a series of monthly payments over the retiree's lifetime (and the surviving spouse's lifetime if this option is selected by the member who, in return, receives a reduced benefit). Most state and local employees are in DB plans that provide cost-of-living adjustments as protection against inflation. In addition, most state and local DB plans provide disability and pre-retirement death benefits.

DB plan benefits are financed by contributions from the employer (and most often from employees as well) and investment income. Employee contributions are usually established at a fixed rate of pay (e.g., 5 percent). Employer contributions are calculated so that, over the long-run (50 years or more), annual contributions plus expected investment earnings are enough to pay the promised benefits plus administrative expenses. The calculations are done by actuaries and designed to maintain employer contribution rates at a level percent of payroll, by smoothing short-term investment fluctuations and using other actuarial techniques.[9] Plan assets are invested in professionally managed, broadly diversified portfolios, with investment fees paid by the plan or employer. Retirement benefits are paid from accumulated contributions and investment earnings.

For employers, a key advantage of DB plans is that investment earnings reduce future employer contributions. In other words, employer and employee contributions generate investment earnings that, in turn, are used to pay benefits that would otherwise have to be paid from future employer contributions. From 1983 through 2002, state and local DB plan investments earned $1.65 trillion, reducing the need for additional employer contributions and taxpayer revenues.[10]

A potential disadvantage of DB plans is that when investment earnings are less than expected, additional employer contributions are required. However, it should be noted that the $1.65 trillion earned by state and local investments over the past 20 years includes investment losses that occurred in 2000 through 2002, as well as in 1987 and 1994.

---

[7] The "2 percent" portion of this benefit formula is referred to as the "benefit multiplier." Benefit multipliers vary, depending on occupation and Social Security coverage. According to the NASRA/NCTR 2003 Public Fund Survey, the median benefit multiplier is 1.85 percent for state and local employees covered by Social Security and 2.20 percent for those not covered by Social Security.

[8] National Education Association, *Characteristics of Large Public Education Pension Plans* (Washington, DC: National Education Association, 2004). The 88 statewide plans surveyed cover 9.4 million active workers. Fifty-seven percent of the plans had vesting periods of five years.

[9] These smoothing techniques work well when investment fluctuations are moderate and short-lived.

[10] U.S. Department of Commerce, U.S. Census Bureau, *State and Local Government Public Employee Retirement System Survey*, 1983 to 2002.

For employees, a key advantage of DB plans is that they provide secure and predictable retirement income over their lifetimes based on pre-retirement earnings. A key disadvantage is that employees who do not remain employed long enough to become vested often lose their DB plan benefits, although employee contributions are usually returned with interest.

HOW DEFINED CONTRIBUTION PLANS WORK

In a DC plan, employers provide employees with individual investment accounts and promise to contribute a certain amount to the accounts (e.g., 4 percent to 8 percent of salary) while the employee is employed. Employees can also contribute to their accounts and decide how the assets are invested, choosing from a number of funds representing major investment categories. Investment management fees are paid from the employee's account, reducing the funds available to pay benefits. At retirement, the employee's benefit is paid solely from the contributions and investment earnings that have accumulated in the individual's account.

For employers, one advantage of DC plans is that the employer's contribution rate is fixed and unaffected by downturns in investment markets. Moreover, the employer has no financial liability for the employees after they retire, even if the DC accounts are insufficient to provide an adequate retirement benefit. (While this may be an advantage for the employer, it is a disadvantage for taxpayers who may have to pay increased public financial assistance as a result.)

A disadvantage for employers is that DC plans may not be a strong incentive for attracting and retaining qualified employees, especially if competing employers are offering DB plans. Moreover, if employees' account balances are inadequate to provide retirement benefits when the employees intend to retire, employers can end up with a number of active employees who are not performing at peak productivity (also known as being "retired in place"). Another disadvantage is that, since the employer's contribution rate is fixed in a DC plan, upturns in the investment markets do not reduce the employer's contribution rate, as they do in DB plans.

For employees, one advantage of DC plans is that the vesting period is typically shorter than for DB plans. Six months to two years is typical. Moreover, DC accounts are easier to transfer if employees change jobs. A major disadvantage is that DC accounts are subject to investment risk and may not be enough to sustain employees throughout their retirement. Another disadvantage is that a high percentage of employees cash-out and spend some or all of their DC accounts when they change jobs, significantly reducing the amounts available to pay retirement benefits.[11]

The remainder of this paper describes the issues and problems involved with replacing DB plans with DC plans.

---

[11] This is surprising since the cashed-out amounts are subject to income taxes. In many cases they are also subject to a 10% penalty tax on early distributions.

DISADVANTAGE # 1:

SWITCHING TO A DC PLAN IS LIKELY TO COST STATE AND LOCAL GOVERNMENTS MORE OVER THE SHORT-TERM. LONG-TERM COST SAVINGS ARE UNCERTAIN AT BEST.

- **DC plans are costly to establish and maintain.** A DC plan must be designed, vendors must be selected, and its operation must be monitored. In addition, employees must be informed about plan features and available investments. Staff time is spent throughout the process, and the sponsoring government must pay additional legal and consulting fees. If a third-party administrator is not hired to administer the plan, the government must do this as well. Even if a third-party administrator is hired, the government will still have operating costs related to the DC plan, possibly ranging in the millions of dollars. For example, the budget for the State of Florida's DC plan, established in 2000, totaled $89 million from FY 2001 through FY 2004. This includes $55 million to educate Florida's 650,000 government employees about the new plan.[12]

- **Pension benefits currently promised to state and local employees and retirees may not be abandoned. Switching to a DC plan does not reduce accrued DB plan benefits already earned.** Most governmental DB plan benefits are protected by the state's constitution or statutes that prevent accrued benefits from being reduced. Consequently, switching to a DC plan is usually accomplished by giving current and future employees the option of remaining in the current DB plan or electing to transfer to the new DC plan. For current DB plan members who elect the DC plan, the value of the member's accrued DB benefit is transferred to the DC plan.

- **When given the option, most employees remain in the DB plan.** In most cases, only a small percent of employees elect to transfer from the DB plan to the DC plan.[13] To increase the number of employees who eventually enter the DC plan, a few governments have restricted the DB plan to current employees and have required newly hired employees to join the DC plan.[14]

- **Even when new hires are required to join the DC plan, long-term cost savings for employers are uncertain and may take many years to realize.** When a DB plan is closed to new hires, it still covers current employees and retirees, and benefits continue to accrue to active employees as a result of service. To the extent plan assets are less than accrued liabilities, unfunded

---

[12] Information provided by the Pension Protection Coalition, based on an analysis of the Florida Public Employee Optional Retirement Program's approved budgets and revenue collections. The analysis was done for the Coalition by the law offices of Olson, Hagel & Fishburn, LLP, January 18, 2005. The budgeted amounts exclude investment management fees paid by plan participants. Used with permission.

[13] Anya Sostek, "Pension Pendulum," *Governing Magazine*, March 2004: 28. Three percent of employees covered by the DB plan elected to join the new DC plan in Florida, 6 percent in Michigan, and 2.5 percent in Ohio.

[14] National Association of State Retirement Administrators, "Overview of Plan Types." Of the 14 state retirement systems discussed in this paper, only two (Michigan and West Virginia) required newly hired employees to join the DC plan. The remaining systems offered DC plans as a voluntary alternative to the DB plan or offered a new plan that combined DB and DC plan features. Available on the NASRA web site (www.nasra.org).

liabilities remain. For DB plans with unfunded liabilities, closing the DB plan to new hires will likely increase the employer's annual required contribution rate. Because new hires are not entering the plan, the cost of funding the liabilities is spread over a declining number of active members,[15] thereby increasing the employer's contribution rate as a percent of covered payroll. In addition, since a growing portion of plan assets must be used to pay benefits, a growing portion of assets will likely be held in short-term securities, thereby reducing investment returns. For example, the Los Angeles County Employees Retirement Association (LACERA) estimated that the County's DB plan contribution rate would increase by 3.66% if employees hired after July 1, 2007, were required to join a DC plan. This would increase County contributions to the closed DB plan by $206 million in 2008. While the contributions would gradually decline over time, the County would have to wait until 2018 to see any savings in DB plan costs as a result of the change.[16]

- **In several cases, states have replaced DC plans due to inadequacy of plan benefits or increased costs.**

  - In 1977, the North Dakota Public Employees Retirement System, originally established as a DC plan in 1966, was changed to a DB plan. Reasons given for the change include the need to provide adequate retirement benefits and the need to attract and retain quality employees.[17]

  - In 2000, the State of Nebraska reviewed its two DC retirement plans for state and county workers and found that between 1983 and 1999 the DC plans' investment returns averaged only 6 percent, compared with 11 percent for the state's DB plans. Recognizing these returns were inadequate to sustain retirement benefits, the state responded by creating a new hybrid plan for state and county workers, combining both DB and DC plan features.[18]

  - In May 2005, West Virginia passed a bill to allow teachers in the Teacher's Defined Contribution Plan (created in 1991) to transfer into the Teacher's Defined Benefit Retirement Plan. According to the West Virginia Consolidated Retirement Board's actuary, the change would save the State $1.8 billion over the next 30 years, because of lower employer contributions required for the DB plan (4.3 percent of payroll) than for the DC plan (7.5 percent of payroll). House Speaker Bob Kiss said, "It actually costs the state more to fund the newer DC [private accounts] system." State teacher representatives said the change would help prevent teachers from leaving their jobs.[19]

---

[15] Governmental Accounting Standards Board, Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* (Norwalk, CT: Governmental Accounting Standards Board, 1994), 7. In situations where a DB plan is closed to new members and unfunded liabilities are amortized as a level percent of projected payroll, projected decreases in active plan members should be included in the calculation.

[16] Los Angeles County Employees Retirement Association, "Proposals to Close Public Defined Benefit Plans." (http://www.lacera.com/home/ProposalstoClosePublicDefinedBenefitPlans.html).

[17] North Dakota Legislative Council, Employee Benefits Program Committee, "Public Employees Retirement Programs – History," October 1998.

[18] Anya Sostek, p. 28.

[19] "Pension Bond Will Benefit Taxpayers," *Charleston Daily Mail.*

DISADVANTAGE # 2:

ALMOST ALL STATE AND LOCAL DB PLANS PROVIDE DISABILITY AND SURVIVOR BENEFITS AS WELL AS RETIREMENT INCOME. SWITCHING TO A DC PLAN WOULD REQUIRE EMPLOYERS TO OBTAIN THESE BENEFITS FROM ANOTHER SOURCE, PROBABLY AT A HIGHER COST.

- **Almost all state and local DB plans provide disability and survivor benefits.** According to the U.S. Bureau of Labor Statistics, 97 percent of state and local government employees in DB plans have disability coverage through the plan and 93 percent may elect joint and survivor benefits.[20] These benefits are largely funded through contributions and investment earnings. Disability and survivor benefits are especially important for employees in hazardous occupations such as firefighters and police officers who may die or become disabled in the line of duty.

- **Few DC plans provide disability benefits. Moreover, DC plan survivor benefits are limited to the participant's account balance.** In the absence of a DB plan, employers would need to obtain disability and pre-retirement death benefits through commercial insurance or else would have to self-fund the benefits. Either of these options would result in additional administrative costs. If the benefits were obtained through commercial insurance, the employer's cost would also include the insurer's profit margin.

---

[20] U.S. Department of Labor, Bureau of Labor Statistics, *Employee Benefits in State and Local Governments, 1998* (Washington, DC: U.S. Government Printing Office, December 2000), pp 94-98.

DISADVANTAGE # 3:

DB PLANS ENHANCE THE ABILITY OF STATE AND LOCAL GOVERNMENTS TO ATTRACT QUALIFIED EMPLOYEES AND RETAIN THEM THROUGHOUT THEIR CAREERS. SWITCHING TO A DC PLAN WOULD LIMIT THIS ABILITY, POSSIBLY PRODUCING OR EXACERBATING LABOR SHORTAGES IN KEY SERVICE AREAS BY INCREASING EMPLOYEE TURNOVER RATES. HIGHER TURNOVER RATES RESULT IN INCREASED TRAINING COSTS AND LOWER LEVELS OF PRODUCTIVITY THAT CAN, IN TURN, RESULT IN THE NEED FOR A LARGER TOTAL WORKFORCE.

- **Employers offer retirement plans as a way to attract qualified employees and retain them so their skills and experience are used efficiently.** According to the Diversified Investment Advisors' Report on Retirement Plans, most large employers see a tangible value in offering a defined benefit plan to their employees – despite the high costs sometimes associated with it. Fifty-eight percent of plan sponsors with 25,000 or more employees believe that their DB plans have a major impact on employee retention.[21]

- **DB plan provisions encourage employees to remain with an employer longer than DC plan provisions.** The vesting period for DB plans is typically longer (e.g., 5 years) than the vesting period for DC plans (e.g., 6 months to 2 years). Consequently, employees have a financial incentive to continue working for the employer at least until they vest. After that, benefit accruals based on continued service provide an additional financial incentive.

- **Key governmental service areas, such as education and public safety, require skilled and dedicated employees to work in positions involving high levels of stress or physical activity or both.** Individuals with the skills and temperament to take on these roles usually have other opportunities in the labor market. DB plans provide strong incentives by rewarding long-term, dedicated service with a secure retirement.

---

[21] "Majority of U.S. Companies That Offer a Pension Plan Say It Impacts Employee Retention," *Business Wire*, September 7, 2004.

DISADVANTAGE # 4:

DB PLANS HELP STATE AND LOCAL GOVERNMENTS MANAGE THEIR LABOR FORCE BY PROVIDING FLEXIBLE INCENTIVES THAT ENCOURAGE EMPLOYEES TO WORK LONGER OR RETIRE EARLIER, DEPENDING ON THE CIRCUMSTANCES. SWITCHING TO A DC PLAN WOULD LIMIT THIS FLEXIBILITY AND MAKE THESE INCENTIVES MORE EXPENSIVE FOR THE EMPLOYER.

- **Governments can use DB plan benefits as a way to manage their labor force by rewarding longer employment or encouraging retirement after a certain period employment.** DB plan benefit formulas can be structured to provide incentives for longer employment by increasing the benefit multiplier after a certain period of service. For example, the formula could provide benefits of 2.0 percent of final average earnings for the first 20 years of service and 2.2 percent for service over 20 years. To encourage retirement after a certain period of employment, DB benefit formulas can limit benefit accruals to a maximum percent of final average earnings or a maximum years of service. In the above example, if the benefit accrual was limited to 62 percent of final average earnings, it would encourage employees to retire after 30 years of service. Other options, such as early retirement incentives (ERIs) and deferred retirement option plans (DROPs), are also available.

DISADVANTAGE # 5:

DB PLANS LOWER OVERALL RETIREMENT BENEFIT COSTS BY POOLING THE RISKS OF OUTLIVING RETIREMENT BENEFITS AND OF INVESTMENT LOSSES OVER A RELATIVELY LARGE NUMBER OF PARTICIPANTS. SWITCHING TO A DC PLAN WOULD REQUIRE EACH INDIVIDUAL TO BEAR THESE RISKS ALONE, CONSEQUENTLY REQUIRING HIGHER CONTRIBUTIONS THAN IF THE RISKS WERE POOLED.

- **DC plan participants must save enough to ensure they will not outlive their benefits while protecting their funds against financial market fluctuations.** Average life expectancy at age 65 is 16 years for men (age 81) and 19 years for women (age 84).[22] Furthermore, 71,000 people will be 100 years or older in 2005, and 1.9 million will be 85 or older.[23] This means that DC plan participants must contribute enough to ensure their benefits will be paid through their maximum life expectancy, i.e., at least until their late 90s.

- **In order to lower investment risk, DC plan participants usually shift a greater portion of their assets from stocks into bonds as they grow older. While this helps protect against equity market downturns, it also lowers likely investment return.** According to a recent Employee Benefit Research Institute study, 401(k) plan participants in their 20s invest 65 percent of their account balances in equities (including company stock) and 21 percent in fixed-income securities, on average. Participants in their 60s invest 49 percent in equities and 40 percent in fixed-income securities.[24] In contrast, large public retirement systems hold 57 percent of assets in equities, 32 percent in fixed-income securities, and the remaining 11 percent in other investments.[25]

- **By averaging risks over a large number of participants, DB plans lower the total costs of providing retirement benefits.** Instead of requiring contributions that are large enough to fund retirement benefits through maximum life expectancy, DB plans only need to fund benefits through the average life expectancy of the group. This lowers required contributions. Moreover, by spreading investment risk over a longer period, DB plans can maintain an investment mix that includes a higher percentage of equity investments. This increases likely investment returns, which further lower required contributions.

---

[22] U.S. Department of Health and Human Services, Social Security Administration, *2004 Annual Report of the Board of Trustees of the Federal Old Age and Survivors Insurance and Disability Trust Funds* (Washington, DC: U.S. Government Printing Office, 2004), p. 81.
[23] U.S. Department of Commerce, U.S. Census Bureau, *Statistical Abstract of the United States 2004-2005* (Washington, DC: U.S. Government Printing Office, 2004), Table No. 12.
[24] Sara Holden and Jack VanDerhei, "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2004," *EBRI Issue Brief*, No. 272, August 2004. Employee Benefit Research Institute.
[25] Keith Brainard, "Public Fund Survey, Summary of Findings, FY 2003," September 2004.

DISADVANTAGE # 6:

DB PLANS EARN HIGHER INVESTMENT RETURNS AND PAY LOWER INVESTMENT MANAGEMENT FEES, ON AVERAGE, THAN DC PLANS. SWITCHING TO A DC PLAN IS LIKELY TO LOWER INVESTMENT EARNINGS USED TO FINANCE RETIREMENT BENEFITS AND INCREASE MANAGEMENT COSTS, TO THE DETRIMENT OF PLAN MEMBERS.

- **Employees direct their own investments in a DC plan, usually selecting from among several funds that reflect major investment categories. Generally, employees have limited investment experience or training.** In a DB plan, investments are selected and monitored by investment professionals who have extensive experience and training.

- **On average, investment returns for DC plans are lower than for DB plans, resulting in significantly lower investment earnings over an individual's lifetime.** According to Boston College economist Alicia Munnell, DB plans outperformed DC plans by 0.8 percent annually, on average, between 1985 and 2001.[26] For a person contributing $5,000 to a DC plan each year for 40 years, the difference between an 8.0 percent annual return and a 7.2 percent return amounts to a loss of over $244,000 in retirement benefits.[27] Other surveys show that individual, non-professional investors may underperform the market by as much as 2.0 percent annually.[28] In the above example, the difference between an 8.0 annual return and a 6.0 percent return amounts to a loss of over $521,000 in retirement benefits.[29]

- **Administration and investment costs for DC plans can be more than four times higher than for DB plans. In DC plans, these costs are borne directly by individual plan participants through deductions from their DC accounts.** According to the Investment Management Institute, the operating expense ratio for DB plans averages 31 basis points (31 cents per $100 of assets) compared with 96 to 175 basis points for DC plans.[30] According to the Illinois Municipal Retirement Fund, the total annual administrative and investment cost for their DB plan amounted to 44 basis points in 1999. If they had switched to a DC plan, total annual administrative and investment costs could have increased up to 225 basis points, or up to $250 million more than the annual administrative and investment costs paid by the DB plan.[31]

---

[26] Alicia H. Munnell and Annika Sunden, *Coming up Short: The Challenge of 401(a) Plans*, (Washington, DC: Brookings Institution Press, 2004), p. 77.

[27] Author's calculations.

[28] W. Michael Carter, Actuary. February 6, 1998. Letter comment on "Pension Liberation: A Proactive Solution to the Nation's Public Pension Systems." Letter is posted on the National Council on Teacher Retirement website (www.nctr.org).

[29] Author's calculations.

[30] Sean Collins, "The Expenses of Defined Benefit Pension Plans and Mutual Funds," *Perspective*, Vol. 9, No. 6, December 2003. DC plan expenses include 12-b1 marketing and distribution fees.

[31] Louis W. Kosiba, "The Defined Benefit vs. Defined Contribution Debate: The $250 Million Question," Illinois Municipal Retirement Fund, October 13, 1999, p. 2. IMRF serves over 360,000 active employees, inactive members, retirees and beneficiaries.

- **DC plan participants often cash-out and spend some (or all) of their DC accounts when they switch jobs. As a result, the accounts contain less money to earn investment returns and to pay benefits at retirement.** According to Alicia Munnell, more than half of DC plan participants withdraw funds from their DC accounts when they change jobs, removing between one-quarter and one-third of total DC plan assets before they reached retirement.[32]

[32] Munnell and Sunden, p. 132.

DISADVANTAGE # 7:

DB PLAN INVESTMENT EARNINGS REDUCE FUTURE EMPLOYER CONTRIBUTIONS. SWITCHING TO A DC PLAN WOULD PREVENT STATE AND LOCAL GOVERNMENTS FROM REDUCING EMPLOYER CONTRIBUTIONS THROUGH INVESTMENT EARNINGS, WHICH CURRENTLY FUND OVER TWO-THIRDS OF PUBLIC RETIREMENT BENEFITS.

- **State and local governments have benefited from investment returns overall and many have used investment earnings to reduce employer contributions.** Over the long-term, an employer's cost of providing DB plan benefits depends on investment earnings. Although investment earnings can fluctuate sharply at times (as happened between 2000 and 2002), over the last 20 years state and local governments have benefited from investment returns and have used the accumulated assets to lower employer contributions. As provided in governmental accounting standards, plan assets that are greater than plan liabilities are amortized to reduce employer contributions.[33] A 2002 survey of Michigan state and local government retirement systems shows that of 115 independent local government retirement plans surveyed, employer contributions for 102 (89 percent) were below the normal cost of benefits as a result of this amortization.[34]

- **Most of the money paid out of state and local retirement plans comes from investment earnings.** Over the last 20 years, state and local government investment earnings amounted to about $1.65 trillion, compared with total employer contributions of $696 billion.[35] This means two out of every three dollars paid from state and local retirement plans was received from investment earnings. According to a paper on state and local retirement plans prepared for the Wharton School's Pension Research Council: **"Setting aside all the other benefits to employers and employees of DB plans, contributions to public pension plans may be among the best investments a state or local government can make."**[36]

  Look at the facts:

  Employer (taxpayer) Contributions = 26%
  Employee Contributions = 12%
  Investment Earnings = 62%

---

[33] Governmental Accounting Standards Board, Statement No. 27, p. 6.
[34] Gabriel, Roeder, Smith & Company, *2002 Michigan Public Employee Retirement Systems Survey*, (Southfield, MI: Gabriel, Roeder, Smith & Company, 2002).
[35] Gary W. Anderson and Keith Brainard, "Profitable Prudence: The Case for Public Employer Defined Benefit Plans," Pension Research Council, Wharton School, University of Pennsylvania, 2004, p. 22.
[36] Anderson and Brainard, p. 14.

DISADVANTAGE # 8:

DB PLANS PROVIDE SECURE RETIREMENT BENEFITS BASED ON A PERSON'S SALARY AND PERIOD OF SERVICE. SWITCHING TO A DC PLAN IS LIKELY TO RESULT IN LOWER AND LESS SECURE RETIREMENT BENEFITS FOR MANY LONG-TERM GOVERNMENTAL EMPLOYEES, INCLUDING TEACHERS, POLICE OFFICERS, AND FIREFIGHTERS, WHO CONSTITUTE OVER HALF OF STATE AND LOCAL GOVERNMENT WORKERS. STATE AND LOCAL EMPLOYEES WHO ARE WITHOUT SOCIAL SECURITY COVERAGE WOULD BE PUT AT EVEN GREATER RISK.

- **Retirement benefits paid from DC plans are significantly less than those paid from DB plans.** The U.S. Congressional Research Service found that, for current older workers, DC-type plans will provide annual benefits of less than $5,000 for half the workers.[37] This is less than one-third of the $18,000 average annual benefits currently paid by governmental DB plans to state and local workers.

- **If average state and local retirement benefits fell from $18,000 to $5,000, it would mean a loss of about $80 billion in annual personal income.**[38] This loss would be felt by state and local economies, since many retirees remain in the same location when they retire. These pension benefits are also, in most cases, subject to federal and state income taxes, thus resulting in a loss of tax revenues. The same would be true in states that rely solely on sales taxes as their source of revenue.

- **The change would have an even greater effect on the 25 percent of state and local government employees who are not covered by Social Security, including about half of school teachers and three-quarters of police officers and firefighters.** When first enacted in 1935, Social Security excluded state and local employees, due to constitutional questions about the federal government's right to tax state and local governments. In 1950, Congress amended Social Security to allow state and local governments to voluntarily elect coverage. By then, however, half of the largest state and local plans had already been established, including many plans for teachers and public safety employees.[39] These DB plans provide benefits that compensate for the lack of Social Security coverage. Replacing them with defined contribution plans would put members at even greater risk, since they would not have Social Security benefits to fall back on.

---

[37] Patrick J. Purcell, "Retirement Savings and Household Wealth: A Summary of Recent Data," Washington, DC: Library of Congress, Congressional Research Service, December 11, 2003.
[38] Based on $110 billion in state and local annual benefit payments made in 2002.
[39] Mitchell, et al, p. 13.

DISADVANTAGE # 9:

DB PLANS HELP SUSTAIN STATE AND LOCAL ECONOMIES BY PROVIDING ADEQUATE RETIREMENT BENEFITS FOR A SIGNIFICANT PORTION OF THE WORKFORCE. SWITCHING TO A DC PLAN MAY SLOW STATE AND LOCAL ECONOMIES, SINCE A LARGE NUMBER OF RETIREES WOULD LIKELY RECEIVE LOWER RETIREMENT BENEFITS.

- **The economic value added by the investment income of state and local DB plans over what would otherwise have been earned in DC plans is estimated to be about $200 billion annually, or 2.0 percent of U.S. Gross Domestic Product.**[40] In essence, state and local retirement plans act as financial engines, using employer and employee contributions to generate investment income that, when paid as retirement benefits, bolsters state and local economies by $200 billion a year. State and local retirees purchase a wide range of goods and services with their retirement income. These purchases, in turn, promote employment and create additional economic demand, generating additional economic activity. As a result of this multiplier effect, the economic activity generated by the higher investment earnings amounts to 2.0 percent of U.S. Gross Domestic Product. As a growing number of state and local employees retire, this percentage will likely increase.

[40] Anderson and Brainard, p. 14.

DISADVATAGE # 10:

SWITCHING TO A DC PLAN IS LIKELY TO RESULT IN PRESSURE ON STATE AND LOCAL GOVERNMENTS TO INCREASE DC PLAN BENEFITS AND PROVIDE ADDITIONAL FINANCIAL ASSISTANCE FOR PUBLIC SECTOR RETIREES.

- **If DC plan benefits are less than what is needed to ensure an adequate standard of living during retirement, continued pressure will be placed on state and local governments, legislators, and taxpayers as retirees outlive their retirement income.** Since DC benefits are not indexed to inflation, extended periods of even modest inflation will mean almost constant pressure for some form of additional financial support for retirees, who will make up a growing portion of the electorate. When DC plan benefit improvements are granted, they will be paid from current government revenues and will not be offset by investment earnings.

CONCLUSION

This paper addresses the question, "Should state and local government defined benefit plans be eliminated and replaced with defined contribution plans?" It concludes that such a move would have significant, long-term, detrimental effects on state and local governments, their employees, their economies, and ultimately the taxpayers.

In the final analysis, the real question is, "How can state and local governments efficiently provide secure and adequate retirement benefits to their employees?" To answer this question, retirement benefits should be viewed in total, including benefits from Social Security, defined benefit plans, defined contribution plans, and individual savings. No single source alone is sufficient, but together they can be used to provide effective and efficiently funded retirement income. Excluding defined benefit plans will only intensify future problems rather than help provide solutions.

Neither market fluctuations nor increased employer contributions should be the driving force for changing the structure of the pension benefits. Instead, decisions should be based on a clear understanding of what outcomes the current design creates and whom it rewards. Retirement plan design represents a significant public policy. Therefore, the plan sponsor contemplating change must understand the policy implications of any new proposal as well as those of the current retirement plan design.

Successful plan changes happen when plan sponsors analyze their current plan and define any problems they discover. When considering such changes, plan sponsors should review several possible actions:

- Survey active and retired members of the current retirement plan.
- Measure the satisfaction and confidence of those members.
- Understand the needs of retirement system employers.
- Understand comparative private sector plans and their goals.
- Adopt a formal policy for the retirement system plan design reflecting the plan sponsor's goals and those of the active and retired members.

Dramatic change is never the answer!

Rather, with the proper analysis and an understanding of the needs of a changing population, fine-tuning of the basic pension plan design can produce excellent results and flexibility for all the sponsors, employees, retirees, and the taxpayers.

NRTA
AARP's Educator Community

Fact Sheet 1
July 13, 2005

TAXPAYERS BEWARE:

A New Pension System Will Be Costly & Chaotic

SUMMARY

Dismantling and replacing the traditional pension system with new private accounts will result in **higher costs for taxpayers** and **bureaucratic chaos**.

Taxpayers will foot the bill for the high costs to transition from a proven traditional pension system to a radical new system of millions of private accounts.

Across the country, there are about 14 million workers who are active employees in the public pension system. There will be **substantial costs** just to shut down the traditional pension, set up millions of private accounts, and educate participants.

For example, in California the estimated transition cost is **$7.6 billion** – and even the most optimistic projections say savings will not be realized for at least 10 years. Los Angeles County actuaries found that the county would not see any net savings for the next 20 years.

Florida modified its traditional system to give workers the option to move to private accounts. After spending **$89 million** to set up these accounts, fewer than 5 percent of the workforce opted to move.

According to an actuary for the West Virginia teacher retirement plan, the new private account system had significantly **higher costs** to taxpayers than the traditional pension system. The actuary also found that switching back to a traditional pension system will save taxpayers millions of dollars annually in pension contributions. **West Virginia switched back to a traditional pension plan.**

On top of these costs, taxpayers will incur a **new direct cost to pay for death and disability pension benefits**. These benefits – critical for police, firefighters and others in hazardous occupations – are part of the traditional pension program, but not for private accounts. Governments will have to pay commercial insurance companies to set up death and disability plans, or fund the plans themselves. Either way, taxpayers pay more.

Setting up and implementing a new system will be complex and chaotic.

Setting up and implementing a new system of private accounts could potentially involve moving millions of workers.

Moving millions of workers to a new system of private accounts will be **chaotic**. In addition, a whole new **complex bureaucratic structure** will be needed to set up and manage these accounts. Educating public sector workers on the private accounts and how to invest will be costly and time consuming. The costs and time lost are better spent providing services to taxpayers.

TAXPAYERS BEWARE:

A New Pension System will be Costly & Chaotic (cont.)

Local, state and national economies will suffer as a result of lower investment returns from private accounts.

Public pensions are an important and continuous source of economic stimulus to every state, city, and town across America. In fact, the traditional system distributes **$120 billion** annually and adds **$200 billion** in economic stimulus each year.

A shift to private accounts will have a dramatic and detrimental impact on local economies because businesses depend upon the stimulus of investment income from the traditional pension system.

Taxpayers can't afford to lose a high quality, experienced workforce.

The traditional pension system attracts and retains valuable and experienced civil servants – many of whom are in vital and high-risk jobs. These workers fight fires, protect our streets, educate our children, and provide medical care.

Many cities and states already have labor shortages and high turnover. A new system of private accounts – with lower, unstable retirement income – will further **diminish the ability to attract and retain a solid workforce** that serves taxpayers – especially for high risk and stressful positions.

Taxpayers will pay for workers who outlive inadequate, unstable retirement income.

Not everyone has the time, resources, or experience to be good investors. Some will win, but **most will lose**. It is unreasonable to expect individual investors to outperform the professional investors who manage traditional pension assets.

Under a new system of private accounts system, many workers will find they have lower and inadequate retirement income**.** Under the current system, public workers' already have modest pensions – an average of $18,500 per year.

For example, in West Virginia, private accounts for teachers have left workers less prepared for retirement – so much so that they switched back to the traditional plan. States that experimented with private accounts saw lower investment returns – nearly a 50 percent reduction.

It is a **risky, guaranteed gamble** to ask workers to bet their entire retirement income on their ability to become investment experts and professional money managers. Transitioning to private accounts is like putting money in the slot machine and hoping to win with three "7s."

We can continue to provide a modest, stable pension to workers who have spent a career providing essential public services. Otherwise, **taxpayers will pay** for public assistance to support workers who outlive inadequate, unstable retirement income.

NRTA
AARP's Educator Community

FACT SHEET 2
July 13, 2005

TRADITIONAL PENSIONS WORK

Don't Destroy a Proven System

SUMMARY

The traditional pension system works – and has for more than 100 years. It is flexible and provides vital services to taxpayers at a low cost. Further, it provides a modest and stable retirement income for workers who have dedicated their career serving the public.

It's a system that works.

For 100 years, the traditional pension system has provided a **modest**, **stable** retirement income for workers who provide **vital services** at a **low cost** to taxpayers.

The system is a proven tool **for recruiting and retaining workers** for critical and often hazardous public sector positions.

The traditional pension system is a **financially sound** approach. These plans **create value** by pooling investment risk and reducing expenses. These benefits – **reducing investment risk** and **administrative costs** – are lost with a system of millions of private accounts.

The system provides the **flexibility** needed by state and local governments to meet the changing needs and demands for public services.

The traditional system provides important **death and disability benefits** for public employees in hazardous occupations – such as police officers and firefighters – who risk death and disability in the line of duty. Private accounts do not provide disability benefits or death benefits to survivors. This is unfair to workers and an added cost to taxpayers.

The private sector also relies on traditional pension plans.

81 of the Fortune 100 companies offer a traditional pension plan, as do 360 of the Fortune 500 companies.

The private sector utilizes traditional pension plans to efficiently manage a large workforce, as well as recruit and retain skilled workers.

TRADITIONAL PENSIONS WORK

Don't Destroy a Proven System (cont.)

Dismantling traditional plans is a costly failure.

States that have experimented with private accounts as workers' primary retirement benefit have found that **a traditional pension plan is a better option**. These states recognized that traditional pension plans are cost effective, efficient, create value, and help workers attain a modest, stable retirement.

For example, **West Virginia** moved from a traditional pension plan to private accounts – and then recently right back to a traditional plan. **Florida**, **Nebraska** and **North Dakota** also found that a new system of private accounts was not a success.

In the end, taxpayers foot the bill for these failed bureaucratic experiments. In California, the projected cost to citizens for switching to a system of private accounts is **$7.6 billion**. Florida spent **$89 million** to set up these accounts, but fewer than 5 percent of the workers moved.

Fix issues rather than discard a solid system.

States have recognized that the traditional pension system is sound. As with any program or system, issues can arise. When necessary, states have taken steps to modify the design of their plans, or to accommodate issues, changing circumstances, and needs.

If your car has a flat tire, repair the tire. Don't waste money on a new car.

If your kitchen sink is clogged, unclog the sink. Don't tear down the whole house.

States are prudent to fix any issues with the traditional system rather than completely dismantling a sound, proven pension system.

Some states have experienced issues with funding shortfalls because they failed to make contributions to the pension fund. **States and local governments should not be surprised when they have to make "catch-up" contributions – just like missing a mortgage payment.** This is the case in states such as California and Illinois. Workers are required to regularly contribute to their pension plans – but employers are not.

NRTA
AARP's Educator Community

FACT SHEET 3
July 13, 2005

TRADITIONAL PENSIONS:
A Tried & True System That Benefits Taxpayers

SUMMARY

The traditional public pension system is the **best way to ensure taxpayers can reliably receive vital services.** It is a **cost-effective, proven and stable method** to attract and retain qualified people to perform critical public sector work.

The system safeguards the delivery of vital public services such as:

- Emergency & First Response – Medical, 911, Disaster Relief
- Police Protection
- Firefighting
- Healthcare Services
- Child Welfare Protection
- Health Inspections
- Forensic Investigations
- Education for Children K-12 and College
- Prison & Correctional Services

Providing a modest pension for public servants helps retain and recruit a strong and experienced workforce needed to continue to provide these vital services. A new system could put at risk vital taxpayer services.

The system is cost-effective.

The traditional pension system is the most **cost-effective** solution to ensure taxpayers continue to receive vital services.

Taxpayers contribute **less than 26 cents for every dollar paid out** in pension benefits. The remainder is funded by investment income and employee contributions. In fact, most state and local workers are required to contribute regularly to their public pension benefit – unlike most corporate pension plans.

The system is proven, stable and efficient.

The current system has worked for **more than 100 years**. It is a proven and critical tool to ensure taxpayers receive reliable services from experienced workers.

The traditional pension system is **efficiently managed** by professionals. There are far lower overhead and administrative costs than a radical new system of millions of individual private accounts.

It provides a **modest** and reliable retirement income for people who have spent a career working for the public good. The average retirement pension is only about $18,500 per year. States that experimented with private accounts saw lower investment returns – nearly a 50 percent reduction.

NRTA
AARP's Educator Community

EXPERT TESTIMONIALS
July 13, 2005

TAKE IT FROM THE EXPERTS

The traditional public pension system is the best way to ensure taxpayers can reliably receive vital services. It is a cost-effective, proven, and stable method to attract and retain qualified people to perform critical public sector work.

"...public pension plans are in a strong position to handle the coming influx of retirees since, unlike Social Security, public pensions are rather well-funded."

"Investing the $2.3 trillion in public pension assets and the flow of benefit payments to annuitants promises a continuous, predictable, and growing source of economic stimulus."

"...through efficient asset management and pooling of resources, public defined pension plans have a significant, positive effect on financial markets."

Source: "Profitable Prudence: The Case for Public Employer Defined Benefit Plans," Pension Research Council, The Wharton School, University of Pennsylvania.

"Another concern raised by defined contribution plans [private accounts] is that it is much more expensive to manage millions of little accounts than one big one. Therefore, under defined contribution plans, too much of the money put into pension savings goes to pay administrative costs instead of pension benefits."

Source: "Protecting the Nest Egg: A Primer on Defined Benefit and Defined Contribution Retirement Plans," The Council of Institutional Investors.

"We've seen from other countries that carving out private accounts from the basic public retirement system doesn't provide enough money for most workers to retire on, and it causes huge financing problems for the basic public program."

Source: "Other Nation's Programs Show Great Risk," Editorial in the *Sacramento Bee.*

"Most retiring workers take their 401(k) [private accounts] distribution as a lump sum. Without an annuity, they risk either running out of money before they die or unnecessarily constraining their standard of living by clinging to this nest egg."

Source: "Coming Up Short: The Challenge of 401(k) Plans," Alicia H. Munnell and Annika Sunden, The Brooking Institution Press.

"There are good reasons for employers to retain a defined benefit [traditional pension system] as the primary retirement benefit for public employees. A defined benefit plan is an effective tool for recruiting and retaining quality employees. Providing a defined benefit plan helps assure a secure source of income for retired employees, reducing the likelihood of these employees relying on public assistance retirement."

Source: "Myths and Misperceptions of Defined Benefit and Defined Contribution Plans," The National Association of State Retirement Administrators.

"Most defined contribution [private account] participants will fall well shy of the estimated 75 percent of pre-retirement income needed to maintain the same lifestyle in retirement."

Source: John Hancock Financial Services Retirement Survey.

"401(k)-style plans [private accounts] were not designed to replace pensions. A 401(k) is not a pension; it's a supplemental tax-incentive thrift plan."

Source: Dan Farrell, professor and compensation expert, Western Michigan University in "Days of Extravagant Pension Plans Fading," *Detroit Free Press.*

"In 401(k) plans [private accounts], we're putting all of the responsibility to save on individual participants, and that can be dangerous."

Source: Amy Monahan, associate law professor, University of Missouri, in "Wither Future Retirees?" *St. Louis Post-Dispatch.*

"[People] will mess up. I'm worried about 20 or 30 years from now. There will be a big problem with elderly poverty."

Source: Robert Schiller, economics professor, Yale University, in "Wither Future Retirees?" *St. Louis Post-Dispatch.*

Individual accounts are a "gamble." "I don't think people really recognize the risk that they're taking."

Source: Steve Dustmann, vice president, McCourtney-Breckenridge & Co., in "Wither Future Retirees?" *St. Louis Post-Dispatch.*

"It actually costs the state more to fund the newer defined contribution [private accounts] system. [By merging back to the traditional system], there are distinct benefits to the taxpayers. The state will experience a large cash flow from the new participants, along with a lowered state taxpayer contribution of 6 percent, down from 7.5 percent. The state will save about $24 million in the first year and there will be a decrease in required taxpayer dollars each year over the next 30 years."

Source: Speaker Bob Kiss, West Virginia Speaker of the House of Delegates, in "Pension Bond Will Benefit Taxpayers; The State Will Save $24 Million in the 1st Year," Editorial in *Charleston Daily Mail.*

STATE AID IN **PRESENT** DOLLAR VALUE FOR NEW EMPLOYEES UNDER A DC PROGRAM

	2005	2010	2015	2020	2025	2028	TOTAL
Alaska, State of	2,419,571	33,708,350	43,996,369	46,925,199	45,266,474	6,596,742	836,993,871
Aleutian Housing Authority	1,361	4,994	6,518	6,952	6,706	4,178	136,281
Aleutians East Borough	1,557	5,711	7,454	7,951	7,670	5,899	156,975
Aleutians East Borough School District	2,654	31,513	41,131	43,869	42,318	7,236	793,065
Aleutians West CRSA	174	2,595	3,387	3,613	3,485	475	64,035
Anchorage Parking Authority	3,185	21,943	28,640	30,546	29,466	8,683	581,359
Anchorage School District	233,622	2,871,807	3,748,302	3,997,826	3,856,510	636,949	72,068,457
Anchorage, Municipality of	410,330	4,543,504	5,930,213	6,324,986	6,101,409	1,118,727	115,028,714
Fairbanks North Star Borough	52,603	416,547	543,680	579,872	559,375	143,417	10,902,337
Fairbanks North Star Borough School District	76,753	736,509	961,296	1,025,290	989,047	209,261	18,899,984
Fairbanks, City of	18,014	278,598	383,824	424,473	416,678	49,113	7,264,035
Homer, City of	13,840	123,706	161,462	172,211	166,123	37,734	3,197,994
Juneau Borough School District	27,963	325,613	424,992	453,284	437,261	76,238	8,207,827
Juneau, City & Borough of	82,163	1,114,901	1,455,177	1,552,048	1,497,186	224,009	27,754,956
Kenai Peninsula Borough	39,334	477,521	623,263	664,754	641,256	107,241	11,995,549
Kenai Peninsula Borough School District	34,645	494,211	645,047	687,988	663,668	94,456	12,243,731
Lake & Peninsula Borough	1,081	14,560	19,003	20,268	19,552	2,948	362,736
Lake & Peninsula Borough School District	5,050	48,363	63,123	67,325	64,946	13,768	1,241,310
Unalaska City School District	2,627	13,766	17,967	19,163	18,486	7,161	370,164
Unalaska, City of	29,541	108,378	141,456	150,873	145,540	80,751	2,947,565
Wrangell Public School District	2,162	20,006	26,112	27,850	26,865	5,895	515,293
Wrangell, City of	7,994	110,531	144,266	153,869	148,430	21,795	2,746,542
Total of All Employers (158 employers)	**4,683,873**	**55,311,800**	**72,267,141**	**77,128,275**	**74,424,134**	**12,921,078**	**1,389,468,066**

Ginny Austerman

From: Ginny Austerman
Sent: Thursday, July 28, 2005 2:12 PM
To: David Teal
Subject: RE: Memo for Ways and means committee

Thank you, David. I will forward this to Rep. Weyhrauch. He is away from his office until August 1st.

I will ask him to respond to you via email, rather than by phone. If we have his thoughts in writing, then there is less chance of missing information or misunderstanding what the committee wants.

I will be working from the Kodiak LIO for the month of August, and back to work on September 6. You can reach me through this email address. When I get set up at the LIO in Kodiak, I will advise you of my telephone numbers.

Hopefully, you will hear from Rep. Weyhrauch early next week.

Thank you for being so thorough with your comments.

Ginny Austerman

From: David Teal [mailto:david_teal@legis.state.ak.us]
Sent: Thursday, July 28, 2005 1:57 PM
To: Ginny Austerman
Subject: Re: Memo for Ways and means committee

My comments at the July 14 meeting of the House Ways and Means Committee were not prepared ahead of time; I just took some notes at the meeting and used them as a basis for my comments. Based on what others said at the meeting and the pre-meeting direction provided by the Chairman, I thought it would be helpful for committee members to know the following:

The State's fiscal situation

This topic was intended to give the committee an idea of the difficulty of filling the retirement system's $5.7 billion unfunded liability. The bottom line is that the state is unlikely to have budget surpluses in the foreseeable future that could make a significant dent in the unfunded liability. In fact, budget deficits are the more likely scenario under the prevalent "no tax increases and no use of Permanent Fund earnings" attitude. There is no easy solution on the revenue side of the fiscal outlook, even with oil at current prices.

A clear definition of "unfunded liability"

I could not speak to this topic because I don't know exactly what "unfunded liability" means or what implications changes to the system might have. I can only point out that making progress is difficult when solution-seekers don't fully understand the issues and problems. It might be nice if the committee knew how the number is calculated, the short- and long-term implications of an unfunded liability and the impact of adopting a defined contribution plan for new employees, how our situation compares to other pension plans (both public and private, using various methods to determine fiscal health), projected trends (including cash flow), options to solve the problem, and advantages and disadvantages

of various options. As it stands, I do not know whether we face a true crisis or a statistical boogeyman.

The potential role of Legislative Finance Division

I stated that we could help in a number of ways (including review of assumptions and/or projections, explanation of reports, and review of potential actions), but needed direction in order to be valuable. This topic is perhaps why Ginny asked me to write down my comments. She asked if I was now clear on the direction of the committee. I had to admit to some doubts that I did not express at the meeting.

You said (before the meeting) that you intended to focus on the future and on solving the system's unfunded liability problem rather than reviewing the legislature's recent actions or trying to assess blame for the fiscal situation. However, the committee spent significant time on the "what did you know, when did you know it and why didn't you tell us" approach to the situation. Should we look forward or backward?

Several committee members expressed a desire for a "one page" perspective of issues. Do you expect committee members to 1) know the issues/situation well enough to propose and evaluate solutions or 2) be briefed on issues and make policy decisions based on recommendations of staff (including Legislative Finance)? Staff reports are not likely to be helpful if we do not understand the expectations of our audience.

I don't know whether you want to discuss these questions at all, let alone at a public meeting, but I am available anytime if want to discuss them with me.

Ginny Austerman wrote:

> David:
>
> Instead of faxing me your memo, would you please email it to me. That way, if Bruce wants it in the packet, it will be easier for
> us to get it into the public records. I am leaving for Kodiak on Friday the 29th. I will be working from the Kodiak LIO and from my home
> there. Terry will be working with me to coordinate data for the committee packets.
>
> Bruce is out of town until August 5, so if you take a few more days to get the memo to us, it's fine.
>
> Thanks, Ginny

David Teal – 9/8 House Ways and Means hearing (FBX)

I'll be talking from a set of 7 charts –

The chairman knows this, but the rest of you don't, I did meet with Rep. Weyhrauch last week and he showed me an article that was cut out of a Nebraska newspaper. The article was on pension plans in Nebraska, and he asked me to create a similar chart for the State of Alaska, that chart is on page 1. The gist of the article, and it's shown right on the graph under the Nebraska School Public Employees Pension Fund, the statement there, like many public pensions, the benefits tend to increase when the fund is flush, contributions go up when shortfalls occur. And then at the bottom of the graph you see a number of actions that the state took, they lowered the retirement age, they increased cost of living benefits, they went to early retirement; those sorts of things. They are blaming that for the problems they are now facing with unfunded liabilities. The good news is we didn't really modify our program in Alaska. There were no cost of living changes, no benefit increases, and no changes of the retirement age. If you look on page 2, you will see the bad news; half of our charts look the same as the Nebraska charts do, maybe worse. The chart's pretty simple, but neither of us were really sure what it meant or what it means. That's not an issue of grasping the size of the $5.7 billion liability, it's trying to figure out what it means. $5.7 billion is twice the annual state budget or ¼ of the Permanent Fund, or if you are into minutia, I guess you could say that if you stacked dollar bills end to end it would go around the earth 21 times. It's a lot of money, but when we figure out what it means, Mr. Chairman,

As Rep. Weyhrauch said, what does it mean to employees, to retirees, to state finances, to communities and school districts among others, that's the question that we face, I think, and let's go with some more questions, why do we have a problem when we didn't do anything wrong? This unfunded liability appeared in a flash, so is it going to vanish just as quickly? Does the state have to take action? What's going to happen if we don't? What actions will have the most impact? So really, I think, this chart is too simple. It's just a snapshot. Pensions are long-term issues. It's better to avoid snap decisions on long-term issues. That's not political advice to the committee, I'm simply recognizing that small differences compound over time, or conversely, that the impact of changes takes a long time to materialize. So, again, more questions, why did the gap appear, where is it headed, are we looking for a solution where none needs to be found? You know why the gap appeared; Melanie (Millhorn) talked about that. Market returns, life expectancy, medical costs; but turn back to page 1 and I really think you see two stories there. School employees see an increase, they see the assets losing steam, we can see that as a change in that dark line, which is their assets. What that means is, they decided to change their assumptions on market rate of return, but the pension which was already increasing rapidly, we didn't show any major jumps like our system did. On the other hand, Omaha Police and Fire Pension Fund shows assets increasing over this period, they don't appear to have been hit by a market downturn, but the benefits jumped tremendously. So, Alaska shows both on page 2, we get a kink upward in benefits, the long-term liabilities, and we get a kink downward in our assets. Where is it headed? Can it vanish, or are we going to continue…..(indisc.) Maybe the members of this task force know more than we do, but neither the chairman nor I knew exactly how this number was calculated, the sensitivity of changing rates – what would this be.

The sensitivity of the rates is one of the things Melanie talked about. So we talked about the dangers of making decisions without knowing exactly where we are and what the projections are on cash flow. The issue being is the system increasing its asset base or are we compounding the problem right now by annual payouts that exceed cash in-flow, and therefore, increasing the size of that liability. In short, rather than looking at a chart like here, we thought we should be saying, "I don't want to look at a chart that looks backward and stops today. Show me a chart of the future, complete with the impact of modifying those assumptions and taking action or not taking action. Tell me whether we face a crisis, or is it just a potential liability that's going to hit us at some point ..... in the future. Describe the consequences of delaying; convince me that this issue is not the same as hearing the Constitutional Budget Reserve will be gone in two years, every single year for the past decade. That's what we have heard there, and how do we know that this isn't the same thing? Last meeting you heard that unfunded liability is a nationwide problem, and you also heard a whole list of things that states are doing about it. You can copy those other states, perhaps you can stumble a solution of your own. I think, and more importantly, the Chairman thinks, that there is a better chance of success in this task force if you really understand the problem and the impact, the pros and cons of each potential action. Then Rep. Weyhrauch asked me to provide more detail on the resources we have to address the problem, more specifically, given the price of oil what are the limitations on the actions we face because we have or don't have money to address it. Turning to page 3, is the financial information; and here I should say that Retirement and Benefits is in a much better position than I am to talk about those questions that I just asked. The issues of sensitivity, and that sort of thing. The Chairman asked me to look at the

overview of the budget, so it's a little more than just PERS, it's sort of a heads-up on what the Legislature may face when they return to Juneau in January. On page 3 you'll see a fiscal summary. That circled number on line 29 of the '06 budget shows that we've got a $2.6 billion budget, and that gives us a surplus on line 30 of about $40 million, but there's a footnote there, and that's oil at $38 in footnote 1, and in particular, look at footnote 4 that says FY '06 appropriations for formula programs excludes $414 million that went to public education. That's because the appropriation for education crossed fiscal years and in doing that, it actually distorts year-to-year comparisons. If we were to adjust for that, the budget is actually at $3 billion. The next chart on page 4 is a chart that is on our website. Typically, what that shows, is the fiscal gap and then at the type of various prices of oil, you can see that at $38 that gap begins to turn into a surplus appearing at the top of the chart. At $38, we breakeven, no gap, no surplus. The current price of oil is $57 and change. That's noted on the charts, and that shows a surplus there of $1.1 for FY '06. Page 5 shows a revised fiscal summary, this is the response to that footnote on page 4 the fiscal note on the traditional summary a footnote to 4. The danger there is that, as I said, the FY '06 budge is really understated by $400 million, and if not for the use of that '05 surplus we would be at $3 billion, breakeven oil prices of $44, and the danger here is that we are not really looking at '06 anymore, we're looking at FY '07, and it's this $3 billion budget that's going to be the base for the '07 budget, not the $2.6 billion that (indisc.).....in the fiscal summary. So what I did was prepare another break-even chart at a $3.5 billion budget. Now you can argue about when we're going to hit $3.5 billion, whether it is '07 or '08 or '09 or '10, but we will get there soon, and you can see on this chart the breakeven point is $53 a barrel, and that $57, where we are at

right now wouldn't give us much of a surplus of $250 million which comes and goes real quickly in a volatile oil market.

The Chairman also asked me to talk about supplemental bids (?), because the idea was how much money those high oil prices in '06 leave us to address the PERS/TRS issue. This is very rough, OMB and the departments are not really willing to talk about supplementals at this time of year, but we've got some guesses. One is the Federal Medicaid matching percentage FMAP. They told us last year, our Senators would try to fix it, and then they argued that everything that we know from the national perspective is that we wouldn't get that money. I think we can now admit that money is not on the way, it's going to cost $55 million in the supplemental bill. Average Medicaid supplementals in the past 5 years have been about $23 million; it wouldn't surprise me if we get another supplemental from Medicaid in that neighborhood.

The Marine Highway System another source of supplemental needs, partly because of fuel, and partly because changes in under funding, $20-25 million may go there. Fires suppression was huge supplemental last year, about $40 million. Fire season's bad this year, as well, but many of those fires are on Federal land this year, and we may get away with no supplemental for fire suppression. Typically, we'll have about $75 million a year for other purposes, or other supplemental needs. I'm looking at a $150-200 million supplemental budget request. What we're looking at here is a true FY '06 surplus of about $500 million (indisc). We'll have cash, but a lot of that, $400 million of it, is carried forward from last year, so bottom line is, you'll have about $900 million on the table available for purposes other than this $150 - 200 million supplemental. Looking to '07, the critical point there is that the starting point of the '07 budget

will be the $3 billion spent in '06 after adjusting for that '05 – '06 crossover. The '07 budget is likely to see increases from that point as always, the FMAP will jump to about $75 million a year, beginning in '07. The state PERS rate increase will cost another $25 million or so, in general funds. If the Legislature again, decides to fund PERS for school districts, that's another $40 million, and if they give the same sort of increase that they gave school districts last year, you are looking at $80 million, so we're up somewhere between $140 to $180 million increase on just those items for '07.

Medicaid – that's probably going to go up as well. It's been increasing at the rate of 14% a year and it's a $600 million budget there, so you are looking at potentially $50-60 million increase, there. In addition to that dividends from Alaska Housing are down, school debt is up. I wouldn't be at all surprised to see a $3.2 or even a $3.3 billion budget in '07. On the other hand, the Capital Budget in '06 was at a little over $300 million and if the Legislature chose to go back to a more normal Capital Budget of $100 – 150 million there is some potential for reduction there. Getting back to the retirement system and how this plays, on this break-even chart you've got $3.5 billion, you've got oil at $53. $57 as break-even there. Where we are in '07 and in the future, all depends on oil. The forecast is now ahead, that occurs in October and the numbers will be released, probably in December. I don't expect an oil forecast above $50. That supports a spending plan of about $3.3 billion, which is, as I just said, wouldn't be a surprise. If all that was a little too confusing about oil prices and so on, there's a summary of that on page 7. Page 7 just shows you General Fund expenditures starting in FY '06 at $3 billion. It increases by $200 million per year. Then it shows how much revenue we would have at $40, $45, $50, $55 and $60 per barrel computes the surplus by simply subtracting the expenditures

and revenues and then tells you what the cumulative surplus is there. You can see that we've got deficits through 2010, even with oil at $50. You need $50 oil just to break even in '07 through '010. At $55 a barrel, you show a cumulative surplus out there, but you're back to an annual deficit by 2010, meaning that you are on the downslide again. The Chairman asked me about a fiscal plan, specifically the role that this unfunded liability may play in that plan, and whether there is any money to reduce the unfunded liability if you choose to do so. If you look at the $55 scenario, you will see that theirs a surplus in '07 of $418 million, which combined with the surplus through '06 of a little over a billion, gives you about $1 ½ billion on the table. Your options range from spending that money all at once; and regardless of how you spend it, it's gone – so I don't think that's much of a fiscal plan, a fiscal plan generally involves not spending money in some fashion, so in order of declining flexibility, you have several options, 1. deposit the money to the Permanent Fund, making it untouchable forever; 2. let it fall to the CBR by simply not (indisc.), because that's the way the system was designed to work, it requires a super majority to pull money out when there is insufficient money to pay for the entire budget, the theory being that the money goes back into the CBR in times of surplus revenue; 3. you can put money towards retirement where it rolls to the very distant future, or you can put money into the public education fund, as you did this year, and that's going to roll the surplus forward to following year.

If you are looking for recommendations here, I would put that '06 surplus into the education fund. Not because it costs us any money, or saves us any money. It just takes the money off the table very early in the process and moves the decision to the full FY '07 process so that rather than going through this abbreviated supplemental process where the

scrutiny is limited, you would put money in the education fund, freeing up that $1 billion or so that is required to go into the education fund. You could then spend it in the '07 budget process. The same amount of money, it just would, in theory then, be given more scrutiny. Even with this, you could pay up to $1.5 billion of the unfunded liability of the retirement system in '07. That's a long way to get to the answer, which is, you do have money to address the problem, not necessarily to fund this gap, but you can make significant progress. So then the question is should you do this, should you fund some of this unfunded liability, if so how much, and what impact would it have on various interest groups? (indisc.) the state's liability is only about half of the systems' liability, so when we talk about a $5.7 billion unfunded liability, about $3 billion of that is the state's. The other $3 billion is the cities, communities and the school districts. Second, we're not going to get a bill for the state, nor will the school districts or the communities ever get a bill for this $5.7 billion, and by that I mean, it doesn't come due in 2017 or 2033 or pick you date out there, because, the way the system works is that the rate increase is designed to eliminate that unfunded liability in 25 years, meaning that you don't have to do anything about it except pay the rate increases, and your problem is solved. Then the primary reason to be concerned about solutions other than rate increases, is that those increases are unacceptable or unaffordable, so I look at it this way, the task force needs to clarify whether you are looking for a solution to the TRS/PERS system wide problem, or simply looking at it from the state's perspective and saying we've got $3 billion of this unfunded liability and that's the solution we are looking for. Are we looking for a solution to the $5.7 billion system wide problem? Then you need to decide whether those rate increases are an acceptable solution, if the focus is the state, I think the rate increases are an acceptable solution, you just increase the operating

budget, the money comes from various fund sources and the critical thing here is that as you saw last year, the state's liability was about $50 million. The general fund portion of that was only $25 million. The other portion comes from Federal and other funds. Now, if we took that $3 billion liability and closed it, making a $3 billion cash injection, you would be spending $3 billion worth of Federal General Funds. That creates a problem, you'll pay for it in rates, in which case the state pays half, and Federal and other sources pay the other half. I guess I would say, why would you want to fix the problem with a infusion of General Funds that cost you twice as much than if you just let it ride. Look at school districts: Anchorage teachers, every teacher, every school..... Teachers are now negotiating for pay increases, but the districts look at it this way, each teacher costs us an additional 5% because of its benefit increase, and we can't afford to increase take home pay in addition to this 5%, and then you've got education advocates saying, "thank you for funding education, but not enough of it went to the classroom." The trouble here is that everybody is right, and in this case, it made may make more sense to pay off the unfunded liability upfront in order to keep rate increases down so that districts aren't faced with the employment dilemma they've got now. The way I look at this, I don't understand how any employer can have a benefit rate of 50%, you hire someone at $50,000 it costs you another $75,000 in benefits, you just can't be competitive, and therefore, because your employees cost you so much, you have to not hire them. The same goes for communities, except the state's not responsible for communities, at least not in the same direct manner as for school districts, so I guess I see this unfunded liability entering the budget debate, really at school districts and communities. The question being whether you want to pre-fund them. You are going to pay now or pay later, you are not going to escape this unfunded liability. From my

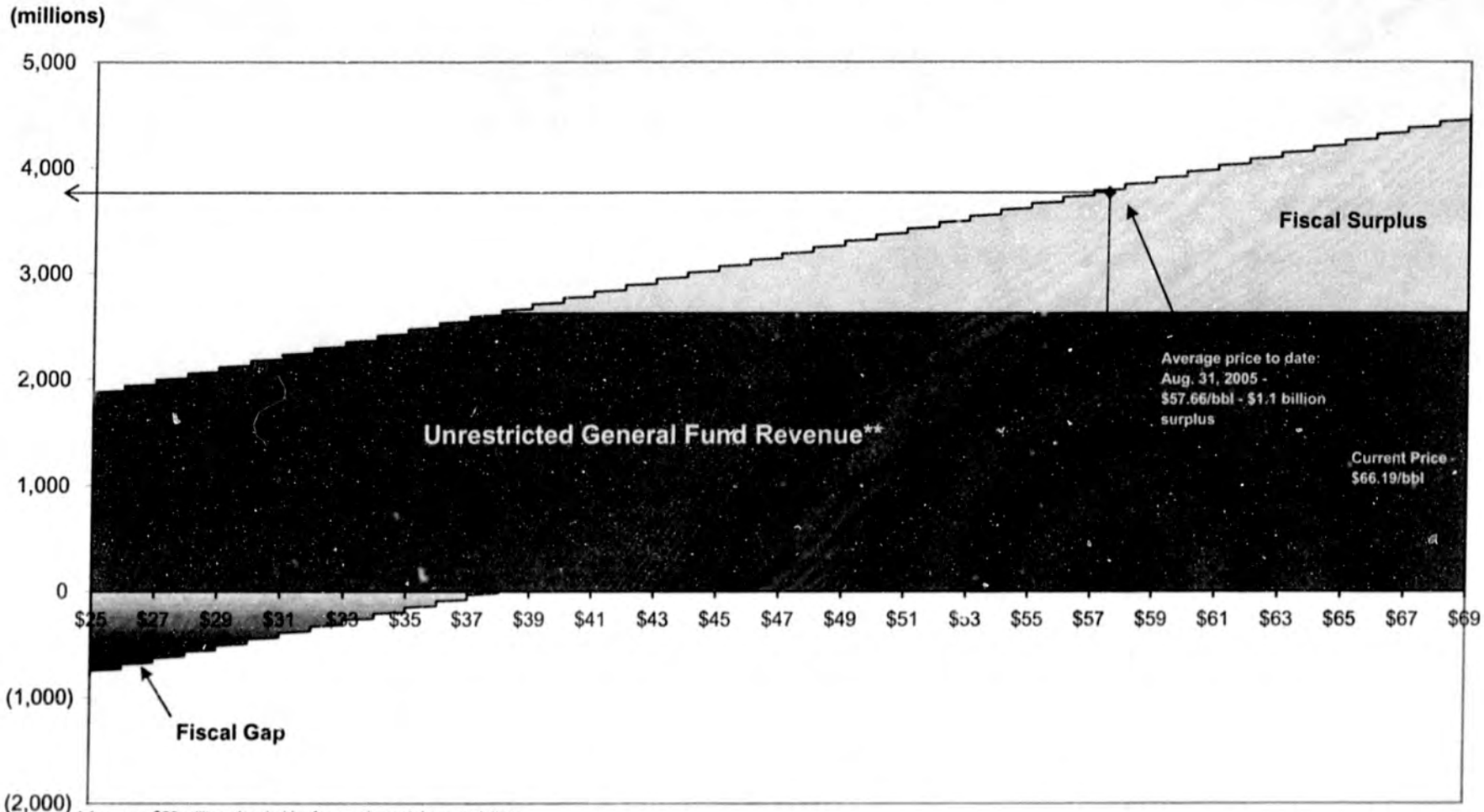
perspective, if you use this surplus in a way of spending it now that starts a new program to increase future spending, you are just compounding the problem. If you use this surplus and put it towards retirement or some other program that's going to cost you now or cost you later, what you are doing is spending the surplus now and reducing future budgets instead of increasing them. My recommendation is that when a surplus exists, use it.

(Here Rep. Weyhrauch asks – "That means letting it lapse into the CBR?

David Teal replies: I would pre-fund, but again, I would pre-fund school districts liability and I would think about pre-funding communities, as I said, you've got no direct liability for communities, but of course, who is it you represent? It's a form of revenue sharing, community assistance, whatever you want to call it. Communities are far less able to afford these 5% increases. If you do that, then the communities which are also hit with fuel cost increases, I guess the logic here is that with high oil prices the primary impact on the state's surplus revenue, we have minor bills, DOT, the University, Troopers that are hit with higher fuel cost, but that's far out weighed by the revenue increase, but high oil prices don't add any revenue to the communities, but it certainly costs them money. That's the only logic I have for saying the communities that need the money and don't have the revenue sources. The state has the revenue sources, and your question in January is "are you going to share with the communities". I don't have any answers, here, I guess we're certainly willing to work with Retirement and Benefits and work with you to try to find the answers, but $5.7 billion's a lot of money, we don't have it all now, and even if we did, there are other things to spend the money on.

From this point on, it's questions and answers.

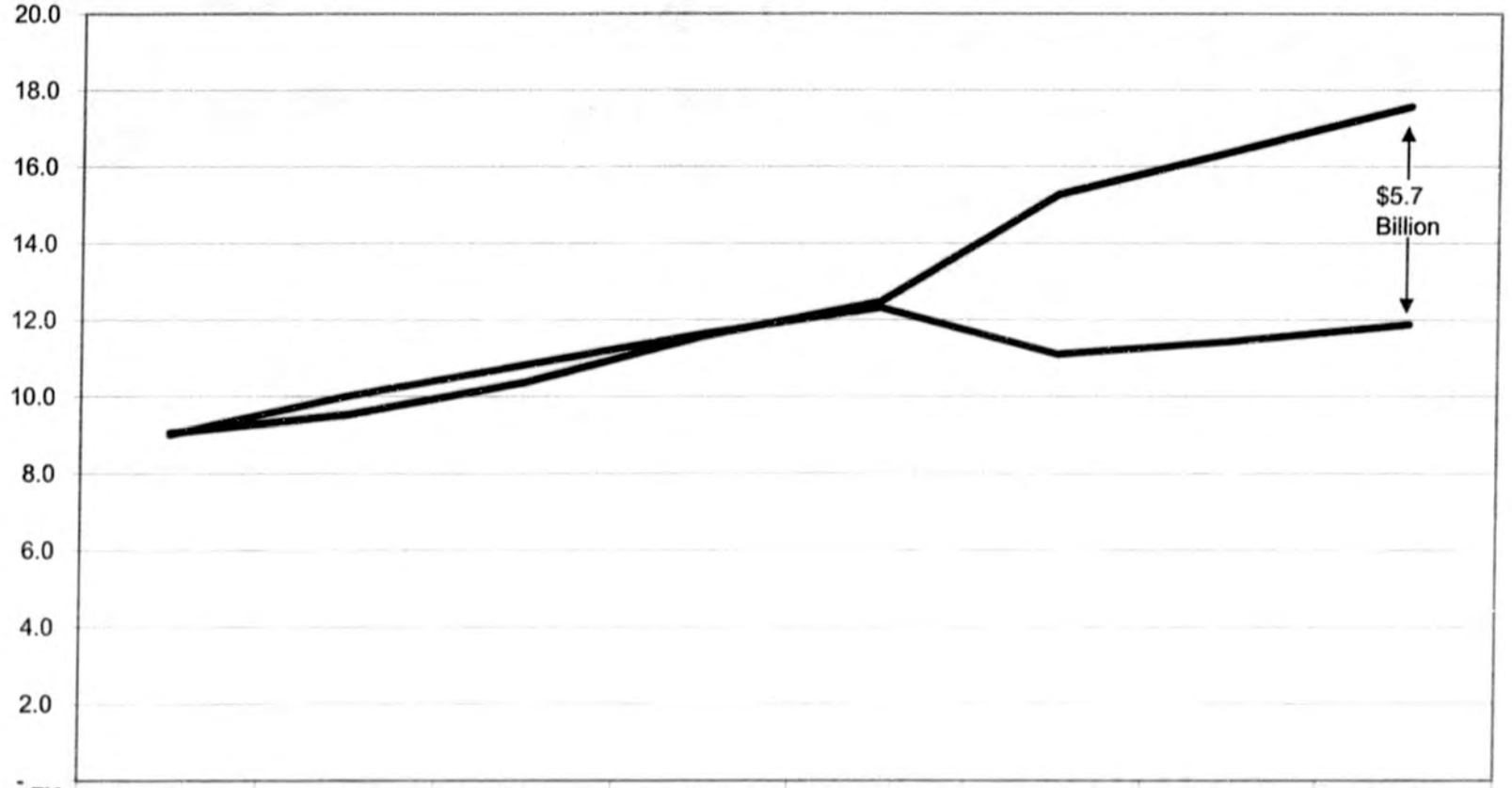
Projected Fiscal Gap/Surplus at Various Year-End Average ANS Crude Prices Given $2.62 Billion FY06 General Fund Budget*



* Assumes $60 million placeholder for supplemental appropriations.

**Includes revenues not directly affected by fluctuations in oil prices. Assumes DOR Spring 2005 Production Projection of .911 million barrels per day.

PERS/TRS
Assets vs. Accrued Liability
(billions)



FY	1997	1998	1999	2000	2001	2002	2003	2004
Assets	9.0	10.0	10.8	11.6	12.3	11.1	11.4	11.9
Liabilities	9.1	9.5	10.4	11.6	12.5	15.3	16.4	17.6

State of Alaska Fiscal Summary

($ millions)

		FY05 Authorized				FY06 Budget (after vetoes)				GF
	REVENUE (Excludes Permanent Fund Earnings)	GF	Federal	Other	Total	GF	Federal	Other	Total	Change
2	Unrestricted General Fund Revenue **(1)**	2,946.9			2,946.9	2,664.0			2,664.0	
3	Revised Revenue Forecast (5/18/05 $43.46/bbl in FY05)	107.8	11.1	6.0				20.0	20.0	
4	Bond Proceeds and Other Borrowing **(2)**			120.0	120.0			330.2	330.2	
5	Corporate Dividends **(3)**			130.6	130.6			114.9	114.9	
6	Retained Corporate Dividends **(3)**			(53.9)	(53.9)			(59.9)	(59.9)	
7	Federal and Other Funds		3,235.3	977.1	4,212.3		2,753.3	851.0	3,604.3	
8	**Total Revenue**	**3,054.7**	**3,246.4**	**1,179.8**	**7,480.8**	**2,664.0**	**2,753.3**	**1,256.2**	**6,673.4**	**(390.7)**
9	**APPROPRIATIONS**									
10	**Operating**	**2,321.7**	**1,633.7**	**1,008.1**	**4,963.5**	**2,214.1**	**1,679.6**	**1,011.2**	**4,904.9**	**(107.6)**
11	Agency Operations (Non-Formula) & RPLs	1,116.4	814.2	1,309.4	3,240.0	1,298.2	819.0	1,345.0	3,462.1	
12	Formula Programs **(4)**	1,150.9	778.3	148.6	2,077.8	845.7	818.7	141.9	1,806.4	
13	Debt Service	2.7	8.6	250.0	261.3	52.0	8.0	241.2	301.2	
14	Fund Capitalization	51.7	32.6	27.7	112.0	18.2	33.9	15.3	67.3	
15	Duplicated Authorization **(5)**			(727.7)	(727.7)			(732.2)	(732.2)	
16	**Capital**	**8.8**	**1,458.8**	**153.5**	**1,621.1**	**338.7**	**1,075.9**	**238.4**	**1,653.1**	**329.9**
17	Project Appropriations & RPLs (Revised Programs)	7.0	1,457.4	101.4	1,565.8	332.2	1,075.9	197.8	1,606.0	
18	Mental Health Projects	1.9	1.5	4.1	7.4	6.5	0.0	5.6	12.1	
19	Projects Funded with Debt Proceeds			95.2	95.2	0.0	0.0	308.2	308.2	
20	Duplicated Authorization **(5)**			(47.2)	(47.2)			(273.2)	(273.2)	
21	**New Legislation**					**11.4**	**(2.3)**	**6.6**	**15.7**	
22	**Total Authorization** (unduplicated)	**2,330.5**	**3,092.5**	**1,161.6**	**6,584.6**	**2,564.2**	**2,753.3**	**1,256.2**	**6,573.7**	**233.7**
23	**Surplus (Draw From CBR)**	**724.2**				**99.8**				**(624.4)**
24	**Post-Session Activity**									
25	Supplemental Operating Appropriations **(6)**	181.2	61.2	20.3	262.7	60.0			60.0	
26	Capitalization of the Public Education Fund **(4)**	414.2	0.0	0.0	414.2				0.0	
27	Supplemental Capital Appropriations	128.8	92.6	74.3	295.7				0.0	
28	Duplicated Authorization **(5)**			(76.3)	(76.3)				0.0	
29	**Total Authorization**	**3,054.7**	**3,246.4**	**1,179.8**	**7,480.8**	**2,624.2**	**2,753.3**	**1,256.2**	**6,633.7**	**(430.5)**
30	**Revised Surplus (Draw From CBR)**	**(0.0)**				**39.8**				
31	Permanent Fund Dividends			532.0	532.0			620.0	620.0	
32	Deposits to Permanent Fund Principal			641.0	641.0		1.7	651.0	652.7	
33	Capital Income Fund			27.0	27.0			30.0	30.0	
34	**TOTAL WITH PERMANENT FUND**	**3,054.7**	**3,246.4**	**2,379.8**	**8,680.8**	**2,624.2**	**2,755.0**	**2,557.2**	**7,936.4**	

Notes:

(1) Revenue assumptions are from the Spring 2005 Revenue Sources Book. The oil forecast is $41.75 per barrel and .920 million barrels per day in FY05 and $38.60 per barrel and .911 mbd in FY06.

(2) Money borrowed for FY05 projects includes $45 million in AHFC bonds and $50.1 million in ASLC bonds. Money borrowed for FY06 projects and debt service includes $62.1 million in revenue bonds, $138 million in Airport bonds, $20.4 million in COPs, $85 million in ASLC bonds and $20 million in line of credit.

(3) Corporate dividends include funds made available to the State by the boards of AHFC, AIDEA, and ASLC. Dividends retained by AHFC for debt service on state capital project bonds are subtracted.

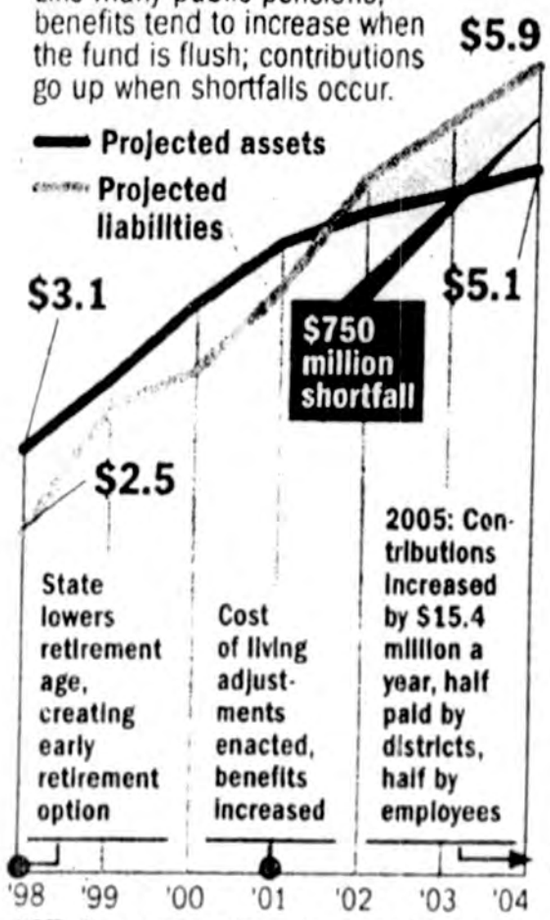
(4) FY06 appropriations for formula programs excludes the $414 million FY05 capitalization of the Public Education Fund (line 26) that will be used for K-12 education in FY06. Appropriating money in one fiscal year while spending it in another distorts year-to-year comparisons. Adjusting for K-12 funding would reduce FY05 GF appropriations to $2.6 billion and increase FY06 appropriations to $3.0 billion.

(5) Duplicated authorizations are in the budget twice, such as when funds flow in and out of a holding account or one agency pays another for services provided.

(6) Supplemental appropriations for FY06 is an estimate

Nebraska school employees pension fund (in billions)

Like many public pensions, benefits tend to increase when the fund is flush; contributions go up when shortfalls occur.



NOTE: Omaha school district has separate fund.

SOURCE: State of Nebraska

DAVE CROY/THE WORLD-HERALD

Omaha police and fire pension fund

(in millions)



2006: Both police and fire benefits increase from 69% to 72%

2007: Both police and fire benefits increase from 72% to 75%

State of Alaska Fiscal Summary

($ millions)

		FY05 Authorized				FY06 Budget (after vetoes)				GF
	REVENUE (Excludes Permanent Fund Earnings)	**GF**	**Federal**	**Other**	**Total**	**GF**	**Federal**	**Other**	**Total**	**Change**
2	Unrestricted General Fund Revenue **(1)**	2,946.9			2,946.9	2,664.0			2,664.0	
3	Revised Revenue Forecast (5/18/05 $43.46/bbl in FY05)	107.8	11.1	6.0				20.0	20.0	
4	Bond Proceeds and Other Borrowing **(2)**			120.0	120.0			330.2	330.2	
5	Corporate Dividends **(3)**			130.6	130.6			114.9	114.9	
6	Retained Corporate Dividends **(3)**			(53.9)	(53.9)			(59.9)	(59.9)	
7	Capitalization of the Public Education Fund **(4)**	(414.2)		0.0	(414.2)	414.2		0.0	414.2	
8	Federal and Other Funds		3,327.9	1,051.3	4,379.2		2,753.3	851.0	3,604.3	
9	**Total Revenue**	**2,640.5**	**3,339.0**	**1,254.0**	**7,233.5**	**3,078.2**	**2,753.3**	**1,256.2**	**7,087.6**	**437.7**
10	**APPROPRIATIONS**									
11	**Operating**	**2,321.7**	**1,633.7**	**1,008.1**	**4,963.5**	**2,214.1**	**1,679.6**	**1,011.2**	**4,904.9**	**(107.6)**
12	Agency Operations (Non-Formula) & RPLs	1,116.4	814.2	1,309.4	3,240.0	1,298.2	819.0	1,345.0	3,462.1	
13	Formula Programs	1,150.9	778.3	148.6	2,077.8	845.7	818.7	141.9	1,806.4	
14	Debt Service	2.7	8.6	250.0	261.3	52.0	8.0	241.2	301.2	
15	Fund Capitalization	51.7	32.6	27.7	112.0	18.2	33.9	15.3	67.3	
16	Duplicated Authorization **(5)**			(727.7)	(727.7)			(732.2)	(732.2)	
17	**Capital**	**8.8**	**1,458.8**	**153.5**	**1,621.1**	**338.7**	**1,075.9**	**238.4**	**1,653.1**	**329.9**
18	Project Appropriations & RPLs (Revised Programs)	7.0	1,457.4	101.4	1,565.8	332.2	1,075.9	197.8	1,606.0	
19	Mental Health Projects	1.9	1.5	4.1	7.4	6.5	0.0	5.6	12.1	
20	Projects Funded with Debt Proceeds			95.2	95.2	0.0	0.0	308.2	308.2	
21	Duplicated Authorization **(5)**			(47.2)	(47.2)			(273.2)	(273.2)	
22	**New Legislation**					**11.4**	**(2.3)**	**6.6**	**15.7**	
23	**Total Authorization** (unduplicated)	**2,330.5**	**3,092.5**	**1,161.6**	**6,584.6**	**2,564.2**	**2,753.3**	**1,256.2**	**6,573.7**	**233.7**
24	**Surplus (Draw From CBR)**	**310.0**				**514.0**				**204.0**
25	**Post-Session Activity**									
26	Supplemental Operating Appropriations **(6)**	181.2	61.2	20.3	262.7	60.0			60.0	
27	Capitalization of the Public Education Fund **(4)**	414.2	0.0	0.0	414.2				0.0	
28	Capitalization of the Public Education Fund **(4)**	(414.2)	92.6	74.3	(247.3)	414.2			414.2	
29	Supplemental Capital Appropriations	128.8	92.6	74.3	295.7				0.0	
30	Duplicated Authorization **(5)**			(76.3)	(76.3)				0.0	
31	**Total Authorization**	**2,640.5**	**3,339.0**	**1,254.0**	**7,233.5**	**3,038.4**	**2,753.3**	**1,256.2**	**7,047.9**	**397.9**
32	**Revised Surplus (Draw From CBR)**	**(0.0)**				**39.8**				
33	Permanent Fund Dividends			532.0	532.0			620.0	620.0	
34	Deposits to Permanent Fund Principal			641.0	641.0		1.7	651.0	652.7	
35	Capital Income Fund			27.0	27.0			30.0	30.0	
36	**TOTAL WITH PERMANENT FUND**	**2,640.5**	**3,339.0**	**2,454.0**	**8,433.5**	**3,038.4**	**2,755.0**	**2,557.2**	**8,350.6**	

Notes:

(1) Revenue assumptions are from the Spring 2005 Revenue Sources Book. The oil forecast is $41.75 per barrel and .920 million barrels per day in FY05 and $38.60 per barrel and .911 mbd in FY06.

(2) Money borrowed for FY05 projects includes $45 million in AHFC bonds and $50.1 million in ASLC bonds. Money borrowed for FY06 projects and debt service includes $62.1 million in revenue bonds, $138 million in Airport bonds, $20.4 million in COPs, $85 million in ASLC bonds and $20 million in line of credit.

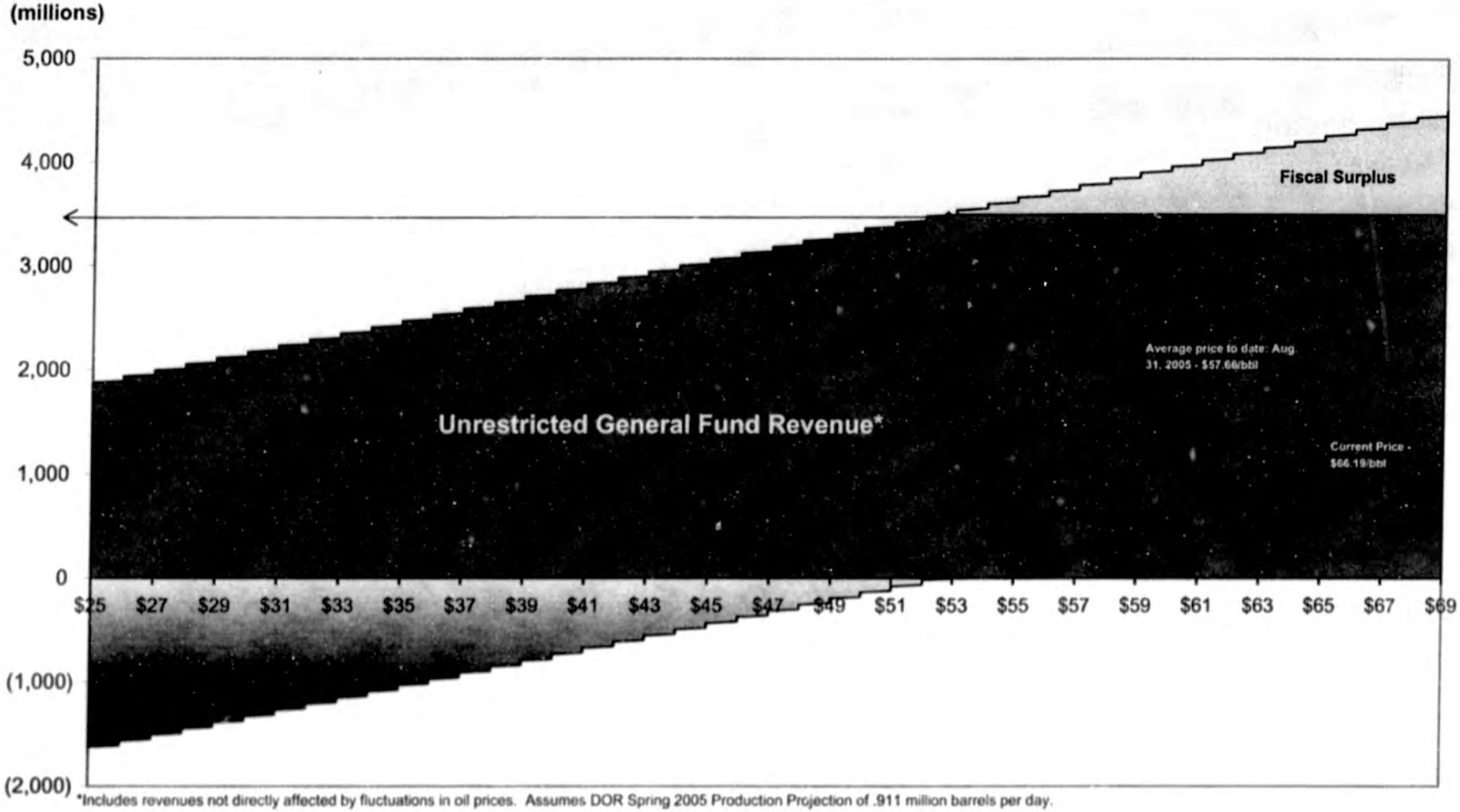
(3) Corporate dividends include funds made available to the State by the boards of AHFC, AIDEA, and ASLC. Dividends retained by AHFC for debt service on state capital project bonds are subtracted.

(4) $414.2 million of FY05 GF revenue will be used for K-12 education during FY06. In order to make cross-year comparisons more meaningful, this version of the fiscal summary shows a transfer of revenue from FY05 to FY06 (line 7) and a transfer of appropriations (line 28).

(5) Duplicated authorizations are in the budget twice, such as when funds flow in and out of a holding account or one agency pays another for services provided.

(6) Supplemental appropriations for FY06 is an estimate.

Projected Fiscal Gap/Surplus at Various Year-End Average ANS Crude Prices Given $3.5 Billion General Fund Budget



*Includes revenues not directly affected by fluctuations in oil prices. Assumes DOR Spring 2005 Production Projection of .911 million barrels per day.

Projected General Fund Expenditures and Revenues

	FY06	FY07	FY08	FY09	FY10
GF Expenditures	3,000	3,200	3,400	3,600	3,800
Oil At $40/bbl					
Revenue	2,725	2,725	2,725	2,725	2,725
Surplus	(275)	(475)	(675)	(875)	(1,075)
Cumulative Surplus	139	(336)	(1,011)	(1,886)	(2,961)
Oil At $45/bbl					
Revenue	3,023	3,023	3,023	3,023	3,023
Surplus	23	(177)	(377)	(577)	(777)
Cumulative Surplus	437	260	(117)	(694)	(1,471)
Oil At $50/bbl					
Revenue	3,305	3,305	3,305	3,305	3,305
Surplus	305	105	(95)	(295)	(495)
Cumulative Surplus	719	824	729	434	(61)
Oil At $55/bbl					
Revenue	3,618	3,618	3,618	3,618	3,618
Surplus	618	418	218	18	(182)
Cumulative Surplus	1,032	1,450	1,668	1,686	1,504
Oil At $60/bbl					
Revenue	3,915	3,915	3,915	3,915	3,915
Surplus	915	715	515	315	115
Cumulative Surplus	1,329	2,044	2,559	2,874	2,989

PERS and TRS Funded Status Report
Alaska House of Representatives
Special Committee on Ways and Means
July 14, 2005

Presented by Joseph Esuchanko, MAAA
Actuarial Service Company, P.C

Unfunded Accrued Liability

1. At June 30, 2004, the combined unfunded accrued liability of the combined PERS and TRS systems was $5.7 billion.

    a. At June 30, 2000, the surplus accrued liability was $63 million.

    b. At June 30, 2001, the unfunded accrued liability was $158 million, a decrease in funded liability of $221 million.

    c. At June 30, 2002, the unfunded accrued liability was $4.2 billion, a decrease in funded liability of $4 billion. In the June 30, 2002 actuarial valuation, the systems' actuary, Mercer Human Resource Consulting, as a result of an actuarial audit performed by Milliman, USA, made significant changes in the assumptions they were using to value the accrued liabilities and in the method of calculating the actuarial value of assets. Therefore, the June 30, 2002 unfunded accrued liability, as calculated, is more indicative of the correct value,

    d. At June 30, 2003, the unfunded accrued liability was $5.0 billion, a decrease in funded liability of $0.8 billion.

2. At June 30, 2002, Mercer projected the unfunded accrued liability at June 30, 2003 would be $4.6 billion, compared to $5.0 billion actually calculated at June 30, 2003. They also projected the unfunded accrued liability at June 30, 2004 would be $5.0 billion, compared to $5.7 billion actually calculated at June 30, 2004. Further, they projected the unfunded accrued liability at June 30, 2005 would be $5.0 billion, and at June 30, 2006, it would be $5.1 billion.

3. At June 30, 2003, Mercer projected the unfunded accrued liability at June 30, 2004 would be $5.5 billion, compared to their previous projection of $5.0. Further, they projected the unfunded accrued liability at June 30, 2005 would be $5.9 billion, and at June 30, 2006, it would be $6.1 billion.

4. At June 30, 2004, Mercer projected the unfunded accrued liability at June 30, 2005 would be $6.2 billion, and at June 30, 2006, it would be $6.7 billion.

5. Using statistical methods, without access to actual assets or liabilities, I project the unfunded accrued liability at June 30, 2005 would be $6.5 to $6.6 billion, and at June 30, 2006, it would be $6.9 to $7.7 billion.

6. The chart on the next page presents these figures in a more easily understood fashion.

7. From these numbers, you can conclude that the unfunded accrued liability is growing at a rate higher than each previous projection.

Progression of Unfunded Accrued Liability, both Calculated and Projected

Date at Which Unfunded Accrued Liability was Calculated or Projected	2000 Calculated (C) or Projected (P) Unfunded Accrued Liability	2001 Calculated (C) or Projected (P) Unfunded Accrued Liability	2002 Calculated (C) or Projected (P) Unfunded Accrued Liability	2003 Calculated (C) or Projected (P) Unfunded Accrued Liability	2004 Calculated (C) or Projected (P) Unfunded Accrued Liability	2005 Calculated (C) or Projected (P) Unfunded Accrued Liability	2006 Calculated (C) or Projected (P) Unfunded Accrued Liability
2000	$-63 million C Note 1						
2001		$158 million C					
2002			$4.2 billion C	$4.6 billion P	$5.0 billion P	$5.0 billion P	$5.1 billion P
2003				$5.0 billion C	$5.5 billion P	$5.9 billion P	$6.1 billion P
2004					$5.7 billion C	$6.2 billion P	$6.7 billion P
2005 Note 2						$6.5 to $6.6 billion P	$6.9 to $7.7 billion P

Notes:

1. Indicates a surplus
2. Projections by Joseph Esuchanko

Observations:

A. From 2002 to 2004, the unfunded accrued liability grew from $4.2 billion to $5.7 billion. That represents 16.5% per year. I project a growth to 2005 of 14.0% to 15.8%.

B. The calculated unfunded accrued liability in 2004 exceeded the 2002 projection by $700 million and the 2003 projection by $200 million.

C. My estimated unfunded accrued liability in 2005 ($6.6 billion) exceeds the 2002 projection by $1.5 billion, the 2003 projection by $700 million and the 2004 projection by $400 million.

D. My estimated unfunded accrued liability in 2006 ($7.7 billion) exceeds the 2002 projection by $2.6 billion, the 2003 projection by $1.6 billion and the 2004 projection by $1 billion.

Alternative Methods of Calculating the Unfunded Accrued Liability

1. The method currently being used is called the Projected Unit Credit method. Under this method, each participant's projected retirement benefit is calculated using the various actuarial assumptions relating to such things as salary increases, expected retirement date and probabilities of death and disability. The fraction of that benefit relative to accrued service compared to ultimate total service is the participant's projected accrued benefit. The liability associated with that projected accrued benefit is derived using actuarial assumptions. The sum of all the participants' accrued liabilities is then subtracted from the actuarial value of assets to determine the unfunded accrued liability. Only 11% of public employee retirement systems use the Projected Unit Credit method.

2. 75% of public employee retirement systems use the Entry Age Normal method. Under this method, each participant's annual normal cost (i.e. the cost associated with that year's accrual) is calculated for each year up to the current year. The accumulated value of those annual normal costs becomes the participant's accrued liability. The sum of all the participants' accrued liabilities is then subtracted from the actuarial value of assets to determine the unfunded accrued liability. Using this method would make it possible to better compare the funded status of the Alaska PERS and TRS to other systems.

3. The Present Value of Accrued Benefits method calculates each participant's actual accrued benefit based on service and salaries to date. It does not use a projected benefit. The liability associated with that accrued benefit is derived using actuarial assumptions. The sum of all the participants' accrued liabilities is then subtracted from the market value of assets to determine the unfunded accrued liability. Using this method determines whether sufficient assets exist to cover actually accrued benefits. This method would not be used to present to unfunded accrued liability for reporting purposes, but would give valuable insight. For reporting purposes, either the Projected Unit Credit method or the Entry Age Normal method would be used.

4. The Aggregate Method, while also not good for reporting the unfunded accrued liability, calculates a total required contribution rate without allocating portions to normal cost and amortization of the unfunded accrued liability. Performing this calculation allows you to determine the appropriateness of calculated funding levels. Under this method, the present value of all projected benefits is calculated. The difference between this present value and the actuarial value of assets is then spread over the future work life of the participants, thus giving the current year's cost.

Future Trend

1. The unfunded accrued liability can be expected to increase over the near future, level out for a period of time, and then begin to decrease as the unfunded accrued liability approaches full amortization. The precise pattern will only be revealed by future events which determine the amounts of benefits paid, the return on investments and the expenses of operating the systems.

Medical Benefits

1. Medical benefits represent a large portion of the systems' benefits paid, accrued liability and normal cost

   A. 28% of all benefit payments to retirees in the year ended June 30, 2004 was for medical benefits.

   B. 38% of the systems' accrued liability is attributable to medical benefits.

   C. 43% of the systems' normal cost is due to medical benefits.

2. The cost of medical benefits increased substantially during the period 1999 through 2004.

   A. National inflation increased 13.1%.

   B. National wages increased 16.7%.

   C. Nationally, average medical premiums increased 67.5%.

   D. PERS/TRS medical premiums increased 82.4%.

3. The growth rate for medical costs far outpaces inflation and continues to grow as a proportion of gross national product.

Recommendations

1. Perform a full actuarial valuation as of June 30, 2005 as quickly as possible.

   A. Use the valuation procedure to determine the sources of the unfunded accrued liability.

      I. First, identify each Tier's accrued liability.

      II. Second, within each Tier, identify each plan benefit's accrued liability.

      III. Use this information to determine strategies for the future.

   B. During the valuation procedure, perform marginal (sensitivity) analyses to understand the future effect on the unfunded accrued liability of experience differing from actuarial assumptions.

      I. Allow the assumptions to vary with respect to health cost trend rates, inflation, investment return and salary increases.

      II. Assume experience both more favorable and less favorable than assumed.

   C. While performing the actuarial valuation, consider alternative actuarial funding methods and assumptions.

      I. Develop the unfunded accrued liability using the Projected Unit Credit, Entry Age Normal, Present Value of Accrued Benefits and Aggregate methods.

      II. Make minor variations in actuarial assumptions.

2. Develop a strategic plan for the future.

   A. Identify ways likely to increase net return on investments.

   B. Study ways to experience medical cost savings.

   C. Determine whether it would be possible to reduce future pension payments without violating the mandate that benefits not be reduced.

   D. Audit operating procedures to develop ways to reduce expenses.

RICHARD J. SOLIE, Ph.D.
482 Slater Drive
Fairbanks, Alaska 99701
Phone: (907) 479-2719
E-Mail: DickSolie@AOL.com

August 17, 2005

Representative Bruce Weyhrauch
Alaska State Legislature
Ways and Means Committee
Juneau, Alaska 99801-1182

Dear Representative Weyhrauch:

Although I understand that the primary focus of your committee's work is the PERS/TRS Funding Shortfall, I would like to make a few comments about the legislature's efforts this past session to deal with perceived problems in the retirement systems that had lead to the current unfunded liability.

First, I believe that the situation facing the legislature was a very serious one, and there was a need for action to both (1) fund the unfunded liability, and (2) fix the retirement systems so as to prevent a future reoccurrence of the problem. The legislature, of course, chose to deal only with the 2nd issue in the last session, and, in my opinion, it took unnecessarily drastic steps which will negatively affect the future ability to recruit and retain future quality employees.

I was a member of the PERS/TRS Tier Committee which had developed a proposal that included major changes in the health plan and a DC/DB hybrid plan for pension benefits. The health care plan in the current PERS Tier 3 and TRS Tier 2 was clearly unsustainable, and I believe the approach adopted by the legislature was a good one – probably superior to that recommended by the Tier Committee. I was, however, extremely disappointed by the decision to create a pension benefit plan for new employees that was 100% DC with no opportunity for choice on the part of new employees.

The legislature was understandably concerned about the future risk involved with the existing plans, but I do not feel that shifting **all** of the pension benefit risk to the employees was reasonable. If you recall, the Tier Committee had requested that the Division of Retirement and Benefits undertake a survey of Alaska public employers, and that survey included questions that dealt explicitly with investment, inflation and longevity risk. There were a combined 126 employers who responded to the risk questions and in all cases **the modal response favored an equal sharing of the risk**. Furthermore, from 63.7% to 68.6% of the respondents (depending on the particular risk

element involved) indicated that the employers share of the risk should be 50% or greater! Despite that, the legislature acted to shift all of the pension risk to employees in the case of future hires. I would urge you, therefore, to consider amending SB 141 to include either a hybrid plan (with both a DC & DB component) or a choice between a DC & DB pension plan. Further, I would suggest that any DB component should contain a "lifetime average earnings" base for calculating pension benefits as was recommended by the Tier Committee.

I indicated above that I felt that the health plan contained in SB 141 was an improvement on the plan recommended by the Tier Committee. I believe that it does a good job of reducing plan costs, balancing the risks between employers and employees, and providing an incentive to future employees to monitor their health care expenses and to be open to plan modifications that would save them and the plan money. Thus, I would recommend that any future modification of the pension plan should retain a health care plan along the lines of that included in SB 141.

Having stated the above, I want to turn to the issue of the Funding Shortfall. In this regard, let me first state my opinion that the ultimate shortfall will turn out to be significantly larger than the $5.7 billion estimate in the June 30, 2004 Mercer actuarial reports. There are several reasons why I am convinced of this. First, the mere fact that, even with the recommended increases in employer contribution rates we are still not covering the interest costs on the unfunded liability, means that it will increase.

Second, the 2004 Mercer report estimates are based on a health cost trend that assumes the combined Medical-Rx inflation rate will fall from approximately 10% in FY07 to 5% by FY14. That assumption is made despite the fact that there is, to my knowledge, no credible evidence to suggest a substantial decline in Alaska or national health cost inflation, and the PERS/TRS medical cost inflation rate has averaged 10% since FY78! Further, it should be remembered that a past understatement of medical inflation was a major contributor (in my opinion, the most significant contributor) to the current unfunded liability.

Third, the June 30, 2004, Mercer report continued to utilize the 1994 Group Annuity Mortality Basic Table for estimating life expectancies. At the time the 2004 Mercer report was prepared, the US National Center for Health Statistics had already released its 2004 mortality estimates (based on 2003 data) and it has since released its 2005 report. The new data indicate that the over-all life expectancy for Americans at birth had increased by 1.9 years from 1994 to 2003, an average rate of more than 2 years per decade! Again, it is significant to note that an understatement of life expectancies was a major element leading to the current unfunded liability. In my opinion, future actuarial estimates should build-in, not only the most recent mortality data, but also the projected long-term trend in future mortality and life expectancies.

Fourth, the 2004 actuarial report continued to assume an average investment return of 8.25% on assets. Past net investment returns have been very close to this average rate, but the current investment climate suggests that a lower rate would be more prudent. A

number of other public pension plans agree with this and have lowered their assumed investment rate of return.

Obviously, changes in the above assumptions would, in an of themselves, increase the unfunded liability, but it would be much better to face that up front than to have a repeat of our recent experience when the current assumptions were belatedly discovered to be in error. Additionally, if the changes made now prove to be overly conservative, future adjustments could be made -- after a suitable time period to establish that the fund is truly dealing with long-term trends -- and such a change would not be painful as would a change in the opposite direction.

Taken together, the above four factors may mean that the $5.7 billion estimate of the unfunded liability may be very significantly low. It behooves the legislature to get the best possible estimate of the actual shortfall so that any "fix" at this time will not need to be repeated in the near future.

With respect to ways of covering the estimated unfunded liability, I do not profess either any extensive study or expertise. This was not an issue with which the Tier Committee or the TRS/PERS boards dealt. Thus my comments in this regard should be viewed as only those of an ordinary, concerned Alaska citizen. That stated, I do have several observations to make, and one of them is that the primary responsibility should fall on the State of Alaska. This is especially true in the case of TRS since the State already recognizes its primary responsibility with respect to education. Nevertheless, a portion of the added cost should, in my opinion, be borne by the school districts and municipalities and in this respect, possibly the already increased employer contribution rates would be a reasonable level for such participation.

Consideration should be given to Pension Obligation Bonds, but the potential negatives of such an approach should be weighed carefully along with the possible interest arbitrage savings. The question of whether these bonds would qualify for federal tax exempt status would, of course be significant, and with respect to such bonds, the sooner a decision can be made, the better, since short-term interest rates are continuing to rise, and long-term rates also appear to be increasing. Of course, if the assumed rate of return on the fund's assets were reduced from the current 8.25%, the potential interest savings would decline. A further question in regard to POBs would, of course, be whether the State should be the primary loan guarantor or whether individual municipalities should be responsible for a portion of their own liability.

From the standpoint of the State of Alaska, it is very fortunate that high oil prices are providing significant unexpected surpluses. It is my strong feeling that the legislature should not fall into the trap of spending those added revenues on further increases in general fund spending. Rather, I feel that a very high priority should be given to dedicating a major portion of those added revenues to covering the unfunded retirement plan liabilities.

In addition to the added revenues, the State, of course, has a significant balance in the Constitutional Budget Reserve which could be used to fund part of the liabilities. Beyond that, consideration may have to be given to drawing on the Permanent Fund – including a portion of the earnings and/or the principal. Since tapping the earnings would probably face strong public opposition, and drawing on the principal would require a vote of the people, public support would need to be developed if these alternatives were considered. In this regard, a ruling from the Alaska Supreme Court as to the State's fundamental obligation with respect to the unfunded liabilities might be helpful.

One final observation that I would make is that -- as many people have already observed - the funds in question are not due today. In fact, a significant portion represents the obligation for retirement benefits due 25 years or more in the future. Thus, it may not be necessary or desirable to pay off the entire amount of the liabilities in the near term. In my opinion, however, it is absolutely essential that the actions taken by the legislature in the coming session provide for funds and commitments that will cover all of the interest (actually lost investment returns) on the unfunded liabilities and begin to make a substantial payment on the principal.

Thank you for your consideration of my comments. If you should have any questions of me regarding the above comments, I will be happy to respond.

Sincerely,

Richard J. Solie, Sr.
Former member of TRS Board
And Member of Tier Committee

Ginny Austerman

From: Rep. Bruce Weyhrauch
Sent: Tuesday, July 19, 2005 9:29 AM
To: Bruce Weyhrauch
Cc: Ginny Austerman
Subject: FW: S.B.141

-----Original Message-----
From: Alyce Hanley [mailto:ahanley@chugach.net]
Sent: Saturday, July 16, 2005 8:53 AM
To: Rep. Bruce Weyhrauch
Subject: S.B.141

Dear Rep. Weyhrauch, I had hoped to tell you how much I appreciated all the work you did on the retirement legislation. I was pleased when I saw you at the luncheon on Thurs., but the conversation was apparently dominated by the gentleman who was convinced that no one should be dependent on Gov't. for retirement plans and everyone should have his/her own retirement account.
I am so thankful my husband wanted a job with retirement benefits after watching all his family of fishermen have little or nothing in their senior years. I have never considered myself dependent on Government, but have been very appreciative that I am financially independent because of Gov't and state pension plans.
I am pleased I was able to serve on the PERS board for almost 2 years. I think retirees were well served by the PERS, TRS and ASPIB boards. Getting rid of those boards was a major mistake in my mind. I realized the finger pointing that Ms. Millhorn referred to was probably all the questions that Pat Wellington asked. There was a concerted effort to get rid of him. He had been on the Board for 27 years and was really dedicated to taking care of retirees and the benefits they had earned. If he had not asked the questions of the AG, I am convinced the $222,000 never would have been returned to the trust fund. He also asked early on what the position of the Div. of Retirement and Benefits was in regard to a defined contribution plan. He was given the run around and then told they had no position since a bill had not been introduced. Of course we learned that Ms. Millhorn had been instrumental in drafting the bill and later stated she was a real advocate of defined contribution plans. They were not honest with the PERS board.
I didn't mean to go at such great length, but again had hoped to be able to chat with you a little and again thank you for your efforts in trying to make this a better piece of legislation. Alyce Hanley

AUG 2 2 2005

August 22, 2005

The Honorable Bruce Weyhrauch, Representative
Alaska State Legislature
State Capitol Room 421

Dear Representative Weyhrauch:

The purpose of this letter is to offer three possible retirement cost containment recommendations. Two of my recommendations could affect the cost of state provided retirement health insurance and one as a possible cost containment method for the retirees optional life insurance, audio, dental, visual, and long term care.

I would hope that you would pass this on to your special committee that is reviewing cost containment for the state health insurance program.

RETIREE HEALTH INSURANCE BUYOUT

Upon retirement tier one employees receive free health insurance for their spouses and themselves, which we both know is extremely costly. It's quite possible that a tier one employee, at the time of retirement, does not need the state provided health insurance, but subscribes to it, because it is free. They may be receiving health insurance because of their spouses employment, military retirement health insurance, or another employee sponsored health insurance.

My recommendation would be that the state explore the benefits of offering, at the time of retirement, an actuarial determined health insurance buyout. This would be a one time payment, which would be binding upon the retiree. This cash incentive I feel could be quite attractive to those retirees that do not need the state provided free health coverage. It would also be my recommendation that if this program is implemented, the spouse and the retiree must sign off on this option as it irrevocable.

I have personally talked to several state retirees who would have been interested in an option such as this at retirement, because their spouses are also covered under a health insurance program. Also I have discussed this concept with a number of tier one employees who that stated they would be interested in evaluating the financial incentives of such a program at the time of retirement.

RETIREE PREVENTION, WELLNESS, AND CASE MANAGEMENT

The above programs may go under different names by a health insurance provider, but basically, are designed to keep the retiree healthy, manage those retirees major medical problems, and contain cost.

Several years ago the PERS and TERS Boards became painfully aware of the escalating health costs. As a result of this, the boards reviewed several options, which if implemented, could reduce costs.

The Boards felt that they could only address one cost containment program at a time. We selected a program to enhance the use of generic drugs by retirees. Involved in developing this program were the Division of Retirement and Benefits, Aetna, Deloitte Consulting [The States Health Insurance Consultant], the PERS and TERS Boards, and RPEA. After a year of developing the program, a formal recommendation was made to the, then director, Guy Bell, which he accepted and implemented. Aetna advised us that for every 1% increase of generic drugs by retirees, could effectively save the program $1,000,000. It is my understanding that this program has resulted in a 5% increase in generic drugs, which saves the system approximately $5,000,000 a year. I point this out to illustrate the success that a cost containment program can have when there is a collaborative effort and not one which the retirees feel is forced upon them by the State or Aetna.

In recent discussions with a representative from Aetna, it was still his opinion that the state could save money on the retiree health insurance cost by implementing the case management, prevention, and wellness program for retirees. I should point out that Aetna has different company names, but they mean the same. The PERS and TERS boards had received, over the past 4 years, numerous presentations, and were prepared to address them and make recommendations by the middle of 2006, of course this will not happen. Aetna has indicated sometimes it is necessary to spend money to save money, but it is their professional opinion, that every $1.00 spent implementing these programs could result in a $2.00 savings.

It is my opinion that implementing new health programs for retirees can only be successful if they feel that this is a cooperative effort, and not something being pushed on them by the state or Aetna. One of the major outside resources that we used when developing the generic drug program was the Retired Public Employees Association of Alaska, through their state president Sam Trivette and his health insurance sub committee. This collaborative effort added credibility to the program and the retirees accepted it.

I am not sure how this credibility is going to be maintained when implementing new cost containment measures because there will be no Boards involved or forum for RPEA to interact with.

If a cost containment program is achieve its goals, once again the retirees have to feel comfortable with the process.

RETIREE OPTIONAL AUDIO, DENTAL, VISUAL, LONGTERM CARE AND LIFE INSURANCE

The above programs are totally funded by the retirees premiums. These premiums are periodically adjusted as a result of claims experienced. There is no mandatory program either through state statute or regulation that requires a timely review process for these optional programs, which has led to overprices premiums for the retirees.

Case in Point: Approximately four years ago the insurance carrier for the optional life insurance program advised the State that the premiums the retirees were paying were out of adjustment and were not necessary to actuarially maintain the program.

Approximately a year and a half ago, the PERS Board and RPEA asked the Division of Retirement and Benefits to make it a priority to review the optional life insurance program for retirees. The Boards and RPEA have received information that many retirees were dropping this program as it became cost prohibitive. The rates for the program could be adjusted yearly and are automatically increased every five years based on age. So the older you get the more it costs. Any rate adjustment can be done just once at the first of the year. And the board and RPEA felt that the review needed to be done before January 1, 2005. At the November 2004 PERS meeting the division provided audited figures which in fact confirmed that for a number of years the retirees had been paying an inflated premium. Based on the divisions figures, and supported by them, the board recommended a 40% decrease in premiums beginning January 1, 2005. This recommendation was supported by RPEA. As I recall possible an additional two million was held in reserve above and beyond what was actuarially required to keep the program solvent. The division stated that they would address this possible over funding before 2006, and make appropriate recommendations to the PERS Board for their consideration and recommendation for possible rate adjustments beginning January 1, 2006. I am not sure how this process will work now.

I know we are all very interested in developing cost containment programs for our State provided health insurance, but I feel the State has an equal responsibility to provide oversight for the optional programs totally funded by the retirees. At this time there is no state statute or regulation that these programs be audited and adjusted as appropriate.

I would recommend that the legislature adopt a statute, or directed the Division of Retirement and Benefits to adopt regulations that require mandatory, yearly review of the financial status of these programs. If not we could conceivable find that once again the retirees are paying inflated premiums. Remember that the optional life insurance premiums can only be adjusted once a year in January. This being nearly September, if an

adjustment is to be afforded to retirees in January, as anticipated, the Division of Retirement and Benefits will have to address this very soon.

I hope you and your committee has found this information useful in your endeavors to contain cost, and if I can ever be of assistance to you and your committee please feel free to contact me.

Sincerely,

Pat Wellington
P.O. Box 1200
Utopia, TX 78884
(830)966-2235
(830)966-2234 [Fax]

June 20 2005

To: Representative Bruce Weyhrauch

From: Gayle W. Harbo
Box 10201
Fairbanks Ak 99710

JUN 2 7 2005

Dear Representative Weyhrach,

I want to thank you for your support of teachers and public employees during the legislative session. My husband and I have resided in Alaska for almost 50 years and we have never seen a more arrogant and uncaring Senate. The rush to push through a poorly crafted bill, Senate Bill 141, which shows little regard for hiring and retaining qualified, dedicated teachers and public employees was a sad comment on what they see needed to build strong communities. We thank you for continuing to oppose this bill which will give no immediate relief to employers but will sentence future employees to an unsure and insecure retirement. It is a bill which benefits the money managers and the private investors and will do little for the communities. Employees and retirees both will take their money and run. There may, in fact, be no retirees living in the state and spending their retirement dollars. This was made clear to me at a retired teachers' meeting - one person said, " If it was my retirement, I would take the dollars and go where it is cheaper to live as I know my dollars might not last for my last years of life."

I have included several things in this packet I am sending. You may not want, or have the time, to use them, but I did want to emphasize the major factors, health care and Mercer's poor advice. There is plenty to support that Mercer erred and the fact that they also advised Fairbanks erroneously is telling. Several members from the three boards, Pat Wellington, Dorothy Wells and Dr. Merritt Olson, have many years of history as do past directors like Guy Bell and Gary Bader, and of course, the Boards' attorney, Rob Johnson, who has a wealth of knowledge. These people are well respected and, above all, honest. The people who served on the three boards, in my short experience, have been honest, dedicated, hardworking and knowledgable. They do not have a hidden agenda and only the best interest in serving the systems' members and earning the best return.

Thank you again for your time and dedication.

Sincerely,

Gayle W. Harbo

Gayle W. Harbo

June 19, 2005

To: Representative Bruce Weyhrauch

From: Gayle W. Harbo, Box 10201, Fairbanks, Ak. 99710, Chair, TRS Board

Re: Committee seeking information regarding PERS/TRS funding ratio

Dear Representative Weyhrauch;

Your interest in resolving the issue of the PERS/TRS situation is heartening and I hope you will contact some of the employees who worked for the Division of Retirement and Benefits for many years with purely the system members' interests at heart. They have the history, the knowledge and the dedication to give you an accurate, honest and complete picture of the problem.

I am including copies of the testimony I gave before the Senate Finance Committee, copies of a letter I wrote to Mr. Bob Boko, Chair of the Joint Tier Committee for TRS and PERS and copies of two articles I wrote regarding the PERS/TERS situation. I know you will get many pieces of information, but observations by current and past Board members may be helpful.

I have been a resident of Alaska since 1957. My husband Sam worked for Fish and Game from 1959 to 1961 and we opened the first Fish and Game office in Nome in 1959. He is now a retired professor of biomathematics from the U of A, Fairbanks and I am a retired high school math teacher, with a BS in mathematics. We have made our home in Fairbanks since 1962. I was appointed to the TRS Bd in 1999 and have been privileged to work with members and members' concerns, particularly in the health care area.

I would like to address three particular areas; some of it is covered in my testimony. Much of what I write is specifically to the TRS system. First I will give a bit of history and then speak to two major problems, Mercer advice and health care, the two main causes of the the reduced funding ratio. I am not an expert, by any means, and so would ask that the loyal former employees of R and B be contacted.

History

As you know the Constitution of Alaska guarantees a Retirement System, not a savings account, to the public employees and teachers of this state. We should be proud of our current fifty year old model system. There are some inequities between TRS and PERS, particularly in the area of Social Security. When teachers were pulled from Social Security in late 50's they were not given the option to establish a separate savings account, as were public employees, with a SBS match of dollars from the state. Also, as you well know, if public employees and teachers not covered by Social Security earn SS

credits by working extra jobs they will be penalized and receive reduced or no SS benefit because of the federal pension offsets, GPO and WEP.

In terms of the current funding ratio, the funds have been there before and at a time when health care costs were not as high. In 1980, the funding ratio for TRS was 67%. In 1980 the employee, the employer and the state each contributed approximately 7%, or a total of 21% of payroll, to the system. Gradually, as the state started to funnel its share through the districts, the employer/state share dropped until, in the 90's the TRS Bd established a rate they hoped to use for 20 years, of 12%. The state seems to have completely forgotten its obligation and in the new legislation speaks only of employee/employer. You will find in FY'02 and '03, Mercer recommended rates lower than 8%, but the TRS Bd stayed with 11% and 12%, respectively. In the spring '97 PERS Bd meeting of Mar 20 and 21, Mercer even suggests that the Boards can retroactively lower employer rates. If the Boards had tried to increase the rates during the years , from '97 to '00, the employers would have screamed because the funding ratios for both systems were at or over 100%.(In the late '70's the state neglected to pay its TRS obligation. With interest, that amount repaid would be considerable)

As you know the Alaska State Pension Investment Board has done an excellent job of earning money for the funds. They look at a five year horizon while the Joint Boards, for actuarial assumptions, look at a 25 year horizon and also must consider health care costs. Michael O'Leary, the Callen consultant to the ASPIB Board, said "how important the time period, when considering investment return performance." It is the reason, that the disparaging remarks of Senator Stedeman were so uncalled for - ASPIB has done a good job and is a good check and balance on the Administration. The newly created ARM Board puts too much power in the hands of the Administration (two Commisssioners) and no elected representation of system members.

MERCER

In copies of my testimonies you will find several references to Mercer, but some of the most blatant errors they made are pointed out in the Joint Meeting minutes of PERS/TRS, Sept. 21, 2004. I enclose a copy of pages 6 and 7. Milliman audited Mercer and as result found significant errors. They also advised Mercer to change the way they recognized gains/losses,from a corridor method to a five year smoothing, which resulted in a significant , one time jump, in the employer contribution rate. The first five years of using this new method is not yet over.

Mercer has advised the Boards for a long time and is the firm which said Retirement Incentive Programs would be cost neutral and then changed their story these past two years. They advised the PERS/TRS Boards on how to deal with "surplus" funds in 2000, while at the same time underestimating health care cost increases and significantly impacting the employer contribution rate due to mortality. In '95 they had used an '84 mortality table when the '94 was available and in 2000, the '94 table . They also , in a March 18 memo to the Division of R and B, attributed hugh costs to the Ad Hoc PRPA, but failed to mention that the largest part of the cost was the settlement of a lawsuit

which made all retirees whole from the beginning of the program. Some members received one time checks as high as $9000.

In speaking with Mayor Steve Thompson of Fairbanks, I learned that Mercer advised the City of Fairbanks on the sale of MUS to GVEA and indicated that the city would suffer no adverse affects. You may know that Fairbanks has huge past service costs resulting from the sale and from MUS workers going from PERS to a labor union. Those workers will now have two retirements and the city is obligated for their pension costs. The same situation recently occurred in Anchorage with Local 302(contact Mayor Sullivan). Mercer has given poor advice to many. Contact Mayor Thompson or Sharon Boko, widow of former city councilman Bob Boko, who also chaired the Tier subcommittee as a member of the TRS Board, to find out the history of this PERS mess. Anselm Staack , former CFO with Retirement and Benefits, is also an excellent, ***honest*** source of this information.

Dollars paid to Mercer have increased from $350,000 in FY'01 to the budgeted amount of $560,000 for FY'06.

Health

As we all know the rising cost of health care is a problem, not only in Alaska, but in every state. The Joint Boards, in the summer of 2000, began an education plan to encourage members in the use of generic drugs. It has been very successful. I have been chair of the Health Subcommittee since 2003 and we have recommended many cost saving methods to the Administration. The Boards can only recommend, not implement. The Administration can make changes to the health care plan , as long as they are prospective - affecting only future retirees. For current retirees they may make changes for convenience or choice, but though they have done this for actives, as in the case of making Providence a preferred provider, they did not do it for retirees. You might ask "why"? Were they waiting, keeping the costs high, until SB141 passed? They will implement a program called "positive enrollment" this fall, claiming it will save $16 million dollars annually on retiree health care. You might ask "why did they wait three years"to implement this cost saving program. In 2003 Retirement and Benefits moved money from the medical reserves, over $20 million, to the funds managed by ASPIB, to get a better return. That left the medical reserves at about $75 million. That figure for '04 is now at $109 million - why are there $30 million in excess reserves.($75 million was considered sufficient in '03). The total amount of reserves for medical, long term care and DVA(the last two are funded by members only) reserves is over $213 million. Anselm Staack, former CFO, has a better grasp of these figures than I do, but the point is, were the high rates quoted inflated? For FY'05 the actual increase in medical cost was 5.5%, down from the 12% of the previous year. Dollars paid to the health care consultants, Deloitte and Touche has increased from $213,000 in FY'01 to a budget amount of $475,000 for FY'06. My other comments on health care are in my testimony, but it is the significant driver in the decrease in the funding ratio and those costs could have been addressed early on by the Administration without resorting to legislation.

Legislation

You are aware that some of the unfunded liability is due to enhancements to current tiers passed by the legislature. The Joint Boards in 2003 and again in 2004 sent letters to

the leaders in the House and Senate requesting that they hold any bills which would provide enchancements and with the exception of the bill that excused the current Commissioner of Education from paying the state back the money he owed when he retired under a retirement incentive, most bills were held back.

In 2003 the Commissioner of Administration, Mike Miller, replaced a very capable, and nationally respected, director of retirement and benefits, with a person with no experience, but with the set agenda to dismantle the retirement system as we know it. Commissioner Miller requested the Boards form a Tier Committee and it was hoped that with the three Murkowski appointees on each board it would be a snap. The Committee was very much managed by the new director, much to the chagrin of Chair Bob Boko. The Committee was indeed a sham to use members' fund money to bankroll a study to be used by the legislature. No committee member recommended a pure DC plan. It was at the insistence of the Administation that Option 2, a pure DC plan, be put in. The committee members, as Dr.Solie said in his testimony, did ***not*** recommend the pure DC plan. All the work done by Mercer, paid for by plan members , as well as all the extra time and energy spent by long time, well respected Retirement and Benefit Division employees, went directly to support the Senate Finance work. The Director spent countless hours working with supporters of any bill which promoted a DC plan , a dismantling of the three Board, more control for the Administration,and less oversight by members of the three boards, several members with over 25 years of service on the boards. Technically, the dollars spent may be legal, but the ethics of those using the funds are questionable. Many long time, dedicated employees of the Division were driven out, moved to other state jobs or resigned in disgust.

When I wrote a letter to the Governor about my concerns, it was answered by the Commissioner of Administration. In May the Boards were told they did not have to meet in June, because Mercer was going to come out with "new assumptions". The PERS Board chose to meet anyway, but the Governor intervened and asked them not to. When Mayor Sullivan told the Governor that Pat Wellington, long time elected member of both PERS and ASPIB, would be in Juneau June 23 for the ASPIB meeting, the Governor said "What's ASPIB?" - a very telling statement.

Thank you, Representative Weyhrauch, for reading my letter and my testimonies (if you have time). My main concern is the quality and longevity of teachers and state employees. I want people to come to Alaska to make their homes, raise children and grandchildren and contribute to their respective communties. SB141, as you well know, does not encourage that, nor does it solve the problem of past service costs for employers. It offers no security. If a person did teach to retirement , he or she would be foolish to stay in Alaska and pay high costs in a harsh climate. Retirees will take the money and run. I wish you luck with your committee and would be happy to help in any way. I would ask you to consult with past, dedicated employees, not the current leadership, if you want a complete and honest picture. I will be visiting my 96 year old Mom for a time, but will be in Fairbanks July 13.

Sincerely

Gayle W. Harbo
sjharbo@yahoo.com

January 23, 2004

To: Bob Boko, Chair, Tier Comm. TRS/PERS
From: Gayle Harbo, member, TRS Comm.

Re: Items for discussion at the Feb. 16 meeting

During the discussion regarding whether a new tier is necessary for either TRS, PERS or both, I hope we will keep in mind some of the reasons for the perceived need and also seriously look at some of the abuses to the systems because of loopholes and/or the ability of non-full time employees to "latch onto a good thing" for the health care benefits. I will list some of my thoughts as a starting point and realize it is in no way a complete list and those of you with more experience with city and borough govt. can add a great deal more.

Some of the reasons for the perceived loss/gain to the systems and therefore a change in the funding ratio:

* increase in health care costs
* increase in the percentage of retirees to actives (TRS, PERS?)
* increase in life span - longer lives (good news), longer draw on systems (bad news)
* impact on prescription drug costs for those over 65 in year "06 and beyond - will the state be reimbursed by Medicare for some share of its expenses.
*districts and boroughs offering early buyouts, increasing final salaries and unfunded liability

Some of the abuses to the systems:

* allowing people who are not full or part time employees of TRS or PERS to contribute minimum dollars , but who then qualify for full health care - help me list them - city and village councils, borough assembly members, legislators , school board members - are there others and am I correct on these? Can we get the places where this occurs and the numbers involved? How many people contribute on earnings of less than $5000 per year and yet are eligible for $9600 per year in health ins. pmts when they retire?
* Employees at the University or school districts who work 9 mo. for most of their careers, then work more than 9 mo. each their last 3 years to "bump up" their average salary.
*School districts which give superintendents and teachers huge bonuses in their final year to "bump up" their average
*allowing TRS employees to vest in PERS and then use the additional years credited to retirement to be paid at the higher TRS average salary

It would be my hope that we would deal with some of the blatant abuses first before considering imposing restrictions on the new employees coming in. Some suggestions to handle the health care abuses and the bump ups would be to:

1. Look at a total service average salary or at least a 10 year average salary
2. Health care benefits are only paid to retired members who have contributed to the retirement system for (then state a minmum number of years and state at least a a minimum annual contibution amt. to TRS or PERS). I do not mean this to include the many PERS employees who work part time for many years, but only those elected officials etc. who see our systems as "the health care gravy train".

Some other thoughts dealing with increased longevity - Maybe 20 years and out is no longer viable. Anyone now retiring at age 42 will most likely draw benefits for longer than they were active contributors.

I would caution considering a DC plan, even in part, for TRS. It has been a disaster for teachers in most states where it has been implemented and most teachers, I am sorry to say, are not wise investors. It may seem paternalistic, but I would much rather see our teachers have a comfortable monthly benefit coming in rather than be faced with drawing out of a DC plan once the market has tanked. We have all heard horror stories these past few years of people unable to retire or people losing their entire retirement savings because of unwise market investments. Three past presidents of NCTR would be available to present information on DC/DB and if we are considering discussing this very important topic I would suggest we request their input and advice. Also Cindee Moore who is the counsel for NCTR is a valuable resource and she would be happy to give us help.

I would appreciate any sharing of ideas and thoughts before the Feb. 16 mtg and look forward to the discusssion. I think it would also be helpful to have data from R and B which tells us the number people who contribute little money annually, but qualify for the health care benefit when they retire. Where did they earn their benefits, who did they work for or serve on some bd or council???

Nov '04
Hartz

Tier Committee

Thanks to the members of the Tier Comm. and to Chair Boko for all the work they have done this past year.

Request of the Administration to form the Committee, not the idea of the Boards.

Reason was ,supposedly, poor earnings the past few years, a declining funding ratio and increasing health care costs.

The Admin and R and B and some Bd members will meet with ASPIB, the investors and monitors of earnings of the TRS and PERS funds Dec.1 to discuss recent earnings. In FY'03 each fund earned over 15%. Over the past ten years the funds have earned an average of slightly more than 9%, above the 8.25% rate of return the Bds have in the assumptions adopted in Dec.2000.

Health care costs are indeed a problem, but in January I addressed a letter to Chair Boko and asked it be entered in the record stating what I called abuses to the system. As we go through this presentation I will ask whether these abuses were addressed and/or considered in the deliberations. Some are:

1. People who are not career employees, but members of school bds, city councils, borough assemblies, legislators etc. who earn small wages for a period of time to vest in either or both systems, then retire and get ,in addition to their small benefit, a health care benefit that costs the system $10000, annually.How many people are on the "health care gravy train"?

2

2.Employees of the university, community colleges, school districts who are hired on contracts, 49% positions (if already retired), as adjuncts etc. These people replace people who would otherwise have full time positions and who would contribute to the retirement system. These people do not contribute to TRS and in some cases are drawing a retirement check and getting health care from the system. How many full time positions has the university lost in the past ten years?

3. Retirement incentive programs and district incentives which increase the unfunded liability and negatively affect the funding ratio. School Bds and the University which allows some employees to "bump up" their salary in their last few years.

4. Employees who only work the minumum time to vest, then retire and get a great health care benefit. The Committee has addressed this in part in that

you have to retire from active status to get health care. It helps with those people who vest in their 20's then do something else and when they retire get health care.

Mercer is our actuary, but we have not always received good information from them. In the early 90's they said the Retirement Incentive Programs would not negatively affect the funding ratio. This past year they changed their story. For the 2000 assumptions they used the 1994 Mortality Table which had a huge impact on the recommened employer contribution rate. Had they used that table in 1995 when the previous assumptions had been adopted the impact wouldn't have been as great. (budget info on the Mercer line item: FY'02 to FY'05 a % increase)

We do not have to go to the legislature to change the health program which is really the only thing that has affected the funding ratio - it is above 90% without health care. Rob Johnson has mentioned at every meeting, sometime several times, that the Administration can make changes to the Health Care Program , without going to the Legislature, as long as they are prospective.

We have several choices today after we hear the presentation.

1. We do not have to recommend either Model
2. We can postpone action until after the Admin and R and B meet with ASPIB
3. We can ask the Admin to adopt some of the changes to Health Care that the two Bds agree on

I look forward to the presentation and the opportunity to ask questions.

article for Retired Newsletter ?)
- Gayle Harbo - Fall '04

Are we in need of another tier???????

In Sept.2003 the Administration requested the PERS and TRS Bds to look at information regarding employee pension benefits to see if a new tier might be necessary. The question is : are we in bad shape financially? The current reports of the ASPIB Board show that earnings for FY '03 were just over 15% each for PERS and TRS investments and the average annual earnings for the past 10 years have been just over 9%, which is above the assumed rate of return of 8.25% for the PERS and TRS funds. For '03 the funding ratio for TRS was 90% without medical and 64% with medical. Health care is a very important benefit. An element which had a significant ,and one-time effect on the funding ratio was the methodology change in recognition of deferred losses - a change from a corridor method to a 5 year smoothing for the recognition of these gains and losses. This impact,alone, in the '03 valuation was 15.03% increase in the recommended employer contribution rate necessary to fund TRS at 100% for 25 years.(See pg. 8 of Mercer's Accuarial Valuation Report, June 30, 2002) The fact is the Retirement System is not going broke - it is in quite good shape considering it is one of only 4 systems which prefunds Health Care.

The actuaries are contracted by the administration to give us information to make reasonable decisions in setting contribution rates, but some of the information provided has proved to be less than reliable. In the early '90's the actuaries, Mercer, assured the Boards that Retirement Incentive Plans offered by the Legislature would have a neutral effect on the funding ratio. Many retirement incentives were offered by the state and by local districts in the '90's.
In 2003 Mercer changed their story and admitted these plans do have a negative effect. The Boards in March wrote a letter to the House and Senate Leaders requesting they not consider legislation which would negativel affect the funding ratio including any Retirement Incentives. Employers and legislators have to accept some responsibility for increased rates. Another significant impact on the recommended employer contribution rate was when the last assumptions were adopted in December of 2000. The assumptions were greatly affected by the increase in mortality as the result of using 1994 Mortality tables. These tables were available in 1995 when the last valuation had been done, but Mercer chose to use '85 tables in '95 thus making the '00 impact greater.

At the first meeting of the Tier Committee, the question was asked about what the purpose of a good retirement system should be - is it to keep costs down for the employer or is it to attract and retain a well qualified and stable work force? The consensus of the

committee seemed to be for the stable, qualified working population. Members of both Boards were interested in seeing some of the abuses of the system changed, such as including huge bonuses in the last year of employment or other arbitrary contributions which cause a huge increase in the average salary for the last years on which the retirement benefit is based. It was also mentioned that the State is not obligated to contribute a match to public employees SBS contributions and ceasing this practice would save the State money.
The Tier Committee has had several meetings this past year, at significant cost to members of the system and the cost for the the acutuaries, Mercer, and consultants, DeLoitte and Touche is way over budget . Mercer was budgeted $400,000 for FY'04, but $552,500 was spent and $580,100 is budgeted for FY'05. D and T was budgeted $340,800 for FY'04, but $432,821 was spent and $$454,400 is budgeted for FY'05.

At the Sept.2004 meeting the Tier Comm. was presented with two Tier Alternatives and I have requested a copy of their minutes from their June meeting and the Sept meeting. At the July meeting , on page 17 of the minutes, the director, Melanie Millhorn, requested that Mercer provide a pure DC plan cost model, though members of the committee, including, Mr. Solie and Mr. Boko stated that a pure DC plan would not meet with approval. The committee members did not suggest a pure DC plan, the Administration did.

The two plans presented place a considerable health care burden on the retiree before age 65 and a burden greater than now on current post 65 retirees. Currently post 65 retirees do suffer a diminishment in benefits as they are required to pay for Medicare Part B which this year is about $800, but will increase almost 20% in January. In calculating the health care monthly premium D and T use a blended rate which comes from pre and post 65 figures, yet Mercer claims (see minutes July 15-16, pg.4) that for purposes of constructing the Tier model they could not split claims between pre and post medicare because the number information is not available, yet retirees must notify the Division of R and B when they reach 65 to tell them whether or not they are Medicare eligible. It would be assumed to get the cost per month of care for pre and post age 65 retirees, they would use total claims in each group divided by the numbers in each group.

I will be going through the two models and will make notes, but the minutes reflect that Jack Kreinheder, from OMB, and Kevin Ritchie from the Alaska Municipal League, thought the system models proposed were not conducive to attracting and keeping a stable workforce. One commented - I wouldn't want to work under this system.
It is imperative to stress that the systems are not in bad shape, but the Administration has been releasing information to paint a bleak picture in hope of getting a new tier through. At the ASPIB meeting in September in Fairbanks, Dorothy Wells made a motion to request the actuaries to compute the funding ratio using the old smoothing method. Other members of ASPIB were also upset about the bad press regarding earnings and they hope to have a meeting with the Administration in early December to talk about their perspective regarding the health of the fund.

WE NEED YOUR HELP - Gayle Harbo Feb 2005

In January, 2005, the Department of Administration presented to the Legislature a plan for a new Tier for both PERS (Tier 4) and TRS(Tier 3), this in spite of a vote by both the PERS and TRS Boards Nov. 19 to "not recommend" a new tier. The plan has two options and each option includes a Defined Contribution component inserted in the plan at the request of the Administration, not the members of the Tier Subcommittee.

We need your help in contacting Legislators on the reasons why a new tier, and particularly a Defined Contribution plan, rather than the current Defined Benefit plan, is not in the best interest of attracting a quality stable workforce. It is interesting that the Tier Plan presented to Legislators included results of the Employer Survey, but not the results of the Employee Survey. Employees surveyed felt a new tier would result in difficulty in recruitment and Tier I employees expressed feelings of guilt that some coworkers doing the same job received fewer benefits. Employees felt retirement health insurance coverage the most important benefit.

How did we get to the point for the Administration to advocate a DC plan? There have been increases in health care costs, but the latest annual increase projected for 2005 is 5.5%, down from 12% in 2004. A special thanks to our retirees for switching to generics and making careful health care choices. The invested TRS and PERS funds had three years of negative investment experience, but in FY'04 both PERS and TRS invested funds earned above 15%, significantly more than the actuary's assumed rate of 8.25%. We have had years of poor earnings before, in the '70's, and recovered to the point that in the fall of 2000 the actuary to the PERS and TRS Boards, Mercer, was advising the Division of Retirement and Benefits on how to allocate assets suplus to 100% funding for TRS and 102% funding for PERS. Also in those years Mercer was recommending an employer contribution rate of 7.09% for FY'002 and 8.29% for FY'03.Fortunately the TRS Board kept the employer rate at 11%, because by 2003 Mercer was recommending an employer contribution rate of 35.57% for FY'05. A significant portion of the recommened 2003 rate increase, however, was due to a change in the method for recognizing gains(losses) and not for actual loss. The TRS Board adopted an employer rate of 16%. Where did Mercer go wrong?? In the early '90's and until last year they insisted the early retirements or RIP's would not affect the funding ratio. They changed their story this year and said that early retirements and "buyouts" negatively affect the funding ratio. This admission came, of course, after the years 2000 - 2003 when the large districts of Anchorage and Fairbanks offered huge bonuses for early retirement and more than 250 people took early retirement. Suddenly $10000 per year per retiree of health care costs was shifted from the school district employers to the retirement system. To

compound the problem, many of these same retirees were rehired the next fall and received a full salary from the district, their retirement check and also had their health care paid by the retirement system. In the assumptions adopted in December 2000 Mercer failed to predict double digit increases in health insurance premiums. In the assumptions presented to the joint boards for adoption they indicated 4 - 5% annual increases. They gave several other poor suggestions, but how can we help now? We do not want a DC plan and need to advise Legislators on some other things that can be done to help the systems recover. The TRS and PERS funds are in good shape compared to most funds in our country , even though we have one of only four systems that prefunds health care. Without medical benefits our TRS system is almost 90 funded.

Here are some things that we need to discuss with legislators. First, they should not be introducing new legislation that enhances benefits for current retirees or active members in the current tiers - any enhancements will just negatively affect the funding ratios of the two systems. The respective boards of PERS and TRS sent a letter to the Legislature in March 2004 to ask them not to pass any introduced legislation that enhanced benefits, yet early in the 2005 Legislature several bills have already been introduced to enhance benefits for special groups. These bills include House Bills 6 and 40 and Senate Bills 21, 24 and 31. The last two seek to remove the sunset on the bill to allow districts to rehire retired teachers while the teachers still draw a retirement salary and have their health care paid for by the retirement system, a $10000 a year drain on the system.

Second, although some of you may not agree, the University and the school districts need to refrain from issuing 49% contracts to retirees. These contracts pull positions, that previously paid in to TRS, from the system. Retirees get the jobs and the districts and University do not have to pay benefits. This increases the unfunded liability, yet the employers are complaining. This happens in PERS positions also, where retirees are hired back, and previous contributing positions are lost. Some Municipalities, Fairbanks and now Anchorage, because of poor management decisions have lost PERS positions to other unions, but still have a PERS liability. They complain, but they are part of the problem.

Third, many groups, school boards, borough assemblies, legislators, city council members put themselves in the TRS or PERS system. They contribute very little, get minimal salaries,but vest and, though they may get less than $10000 per year in retirement they receive more than $10000 a year health care benefit. There are almost 8000 recipients in the PERS and TRS systems who received minimum benefits. These are loopholes that need to be closed.

Why is a defined contriution system proposed by the Administration not a good thing? As Alyce Hanley of PERS and Dick Shultz of TRS so eloquently stated, now is not the time. Why should future retirees be burdened with a new tier or a DC plan because of Mercer's poor advice and poor judgement on the part of some employers. We want to attract new, young workers to Alaska and we want them to stay. Salary is no longer a draw. The Job Fairs that used to have 5 and 6 applicants for every job now have empty rooms. People can go to places where weather is better, the cost of living is cheaper and

they can get higher wages. Alaska is no longer at the top of the list. If we want to attract new and vital young people to Alaska we need a good retirement system, one that assures security in old age. We are already losing many people because of the GPO/WEP pension offsets which reduce or eliminate any Social Security benefits we may have earned.

Seniors who work and retire in Alaska deserve more than a risky DC plan that does not guarantee a lifetime income, has no cost of living provision and may require, if a senior suffers a stroke or alzheimer's disease, that some stranger would manage the lifetime DC benefit which they would get as a lump sum. In Governor Murkowski's letter to seniors in December 2004, he states that "Alaska's future also depends on the health and well being of our people and communities." Let us keep that promise to Alaska's seniors and our future retirees and not adopt a new tier and , definitely not, a DC plan. A Defined Benefit plan, which we now enjoy, is the way to keep and attract qualified, long term employees whose children and grandchildren will be Alaska's future.

Testimony - Gayle Harbo
Senate Finance
Mar. 29, 2005

Good afternoon. My name is Gayle Harbo and I have been a resident of Alaska since 1957, most of the time living in Fairbanks. I taught in Fairbanks for 25 years, most of the time at Lathrop High School and was Chair of the Math Dept and Advanced Placement Coordinator for almost 20 years. I am here as a member of the Teacher Retirement Board. The joint boards thank Senator Stedeman for his willingness to teleconference with us on Friday Mar. 25. We are sorry his plans changed but since he could not teleconference hope he and the Committee will read the verbatim transcript of the morning's discusssion so they realize the depth of true concern that each Board member has regarding all the bills which seriously impact a retirement system which has worked well for 50 years. The only significant changes that have been made in recent years have been enhancements of benefits due to legislation. The Joint Boards have sent letters to the Legislature these past two years asking that you not introduce any bills which enhance benefits and the Administration has agreed to testify against these bills because all would increase the unfunded liability.

I am going to address 3 topics in my remarks and will be happy to answer any questions. If I don't know the answer I will try to find out.

My first issue is the interaction of the 3 Pension Boards. As you know the main work of the TRS and PERS Boards is listening to appeals of members, recommending employer contribution rates and adopting actuarial assumptions every 5 years based on the recommendations of the Commissioner of Administration and the actuary. ASPIB manages and invests the contributions to the system. The Joint Board members have great admiration and respect for the way ASPIB and the staff of Revenue ,who work with Gary Bader , invest and care for our funds. Over the past 10 years the funds have earned almost 9% annually, at or near the assumed rate of our actuary. Earnings are not the problem causing the unfunded liability.

This leads to my second issue. The main driver of the decrease in the funding ratio has been the rapid increase in health care costs., a problem not unique to Alaska.You have seen in past presentations that without the inclusion of medical costs the funding ratio is a respectable 91% for TRS and 120% for PERS. Health care costs have accounted for 50% of the employer contribution rate increases in past few years.The Administration can make changes in the Health Care plan without legislation. First, changes can be made to the plan for current tiers if they do not diminish benefits, but are a matter of choice or convenience.(An example would be requiring members use hospitals, both in and out of Alaska ,which are preferred providers so

significant savings could be negotiated - Providence in Anch. is not a PP yet over 80% of retirees go there, the hospitals in Juneau and Sitka are owned by their respective cities. They are not preferred providers and there is little savings to the state.)Secondly, signifcant changes can be made to the plan for employees hired after a specific date.

About 5 years ago the Joint Boards recommended an education program to encourage members to use Generic Drugs. The members responded and now 42% of the drugs used are generic. Every percent of brand name drugs replaced by generics saves the plan 1M.(see Oct.'04 Newsbreak). The Health Care Committee has for several years recommended the state pilot a disease mgt. program, particularly for diabetes, but we were told that the start up cost of $240000 was too much. In speaking with other health plan administrators who utilize disease mgt. I have been told that the cost savings in the first four years are considerable and would more than recoup the start up costs. Mr. Mike Humphries, from the benefits division at the U of A, the NEA Health Trust and ,perhaps Mr. Jarrell,our new trustee from Bering Straits School District, indicate their plans incorporate this element. For retirees this past year, 474 members had claims of over $50000 each and accounted for 53M of the medical expenses to the state plan. Surely disease mgt could have reduced some of this cost. Other than the generic drug campaign no substantive cost savings measures have been taken. The Health Care Committee has presented a list of several cost savings measures that we, and the entire Jt Board, would like to see initiated. The Boards can only recommend, however, not implement. I feel we would not be at this juncture, with drastic changes recommended to the system, if this Administration and past Administrations had held a Forum with employers,legislators, representatives of unions and the Municipal League and medical professionals to discuss methods of resolving these skyrocketing costs. We all recognize the problem and would like to be part of the solution, not adversaries. Senator Seaton has a bill regarding generics and closed formularies. This does not have to be legislated - the Administration can make those changes now as long as they do not diminish benefits to the current tiers.

My third issue deals with the comments by some that the Boards have not been responsible in recommending the employer contribution rate and with the awarding of the ad hoc PRPA. Wrt TERS and the employer rate, it is a

recommendation, the Administration can set the rate higher. The Boards act with information provided them by the Administration and the actuary. In the early '90's the TRS Bd adopted a 12% employer rate and to ensure stablility for employers for future planning, they intended this rate be used for at least 20 years. In 2000 and 2001, however, when setting the rates for FY'02 and FY'03, Mercer, our actuary, recommended rates as low as 7.09% and 8.29% for those fiscal years. The TRS Bds did, in those two years, drop the rate to 11%; had they not, the employers may have been upset. In '03 we set the rate at 16%, though the first motion was for 17%. The contribution rate has been higher - in FY' 83 and '84 the combined rate for state and school district was close to 18%. When I started teaching in the '60's, employee, employer and the state each contributed 7%. The employee population at the University that is not under TRS, but under private accounts has a match by the employer of roughly two to one.

The other issue of Ad Hoc PRPA's apparently needs to be clarified since you were given a paper dated Mar. 18 from Mercer regarding the funding status due to plan changes, mostly enhancements through legislation, and Ad Hoc PRPAs. As you know the Boards recommend Ad Hocs on the basis of information provided by the actuary and the Commissioner of Administration. The Boards have only made recommendations when the funds were healthy. No Ad Hoc has been recommended since 2003. A retiree gets either the Ad Hoc or the automatic PRPA, not both. In the past years when the Ad Hoc has been awarded it only causes a small "blip" in the increase of the employer contribution rate, probably less than .06%. The Mar. 18 letter fails to indicate that probably 99% of the ad hoc cost mentioned, resulted from the settlement of a lawsuit in the mid '90's. The state lost the lawsuit and as a result had to make all retirees whole, from the time they retired, wrt the PRPA. The dollars paid out include not only past prpas but the interest earned. Many individual retirees who had been retired 30 to 40 years received checks close to $10000. The lawsuit, as many of you may remember resulted because past administrations had not awarded a prpa when the fund was "healthy".

The Mar. 18 letter also attributes nearly 1B of the increase to the unfunded liability to benefit enchancements by the legislature. The Boards have said many times that "tinkering" with the tiers, once they have been established has not been in the best interest of the funds and for some of

these changes the actuary has not accurately predicted the rapid rise in health care costs. In the assumptions adopted by the Boards, the last time in Dec. of 2000, Mercer had a Medical assumption rate of 5.5%. We now know was not a realistic assumption. The Boards requested an Actuarial Audit in 2001 and the resulting report indicated that we should look at Medical assumptions on an annual basis. You also know that the RIP programs advocated by the Legislature in the early '90's were to be cost neutral, but this past year Mercer indicated they have had a negative affect on the funding ratio, primarily because of escalating Medical costs. Despite this poor advice, if you examine Mercer's budget line item over the past few years, you will see there has been a 100% increase in their fees.

I thank you again for your time and hope you will carefully consider whether drastic measures need to be taken at this time. We all agree there is a problem and we hope by working together we can begin to solve it, but please do not burden future hires for the mistakes of others. Changes can be made, without legislation, to control current and future costs. Please let us work together to make Alaska continue to be the place young people will want to come to work, as you and I once did.

Testimony turned in to Senate Finance - Mar 30, 05

Good Morning . My name is Gayle Harbo and I have been a resident of Alaska since 1957. I am a mother, a grandmother and a teacher and most recently a member of the Teacher Retirement System Board. As a parent and a grandmother I am most concerned about the quality and stability of the education employees in the state of Alaska. When I came to Alaska there were many applicants for each job, with prospective teachers often subbing for years before they were hired to a permanent position. Salaries in the late '60's and early '70's were very competitive. That is no longer true. I believe teacher job fairs are no longer held in either Anch or Fairbanks. The point is, Alaska is no longer the place to come to get a good salary . A friend in Wasilla said if she had stayed in Wisconsin for her teaching career she would have a better retirement then she will have here.

I want the best and brightest to teach my grandchildren. To attract teacher's it is important we keep the DB system. Many of the changes recommended by the Tier Subcommittee of the Joint BDs could be adopted without going to a defined contribution system. One, in particular, would change the number of years over which an average salary is computed.

It is important to realize that, under the proposed system, seniors would be given a "pot" of money when they retire and then have to manage a resource that is to last them for a lifetime in terms of annual income. They would have no inflation proofing(PRPA, which even SS provides)and they would be at the mercy of investment advisors and unknown investment costs. As individuals, they would not be able to get the breaks ASPIB gets by investing large sums of money, putting their dollars at even greater risk. You have all read the horror stories of retirees who have lost everything because they did not have the expertise to invest. Most are emotional, not long term investors and their resources may not match their lifetime expectancy.

Another issue for seniors is health. I personally know many seniors who have suffered from stroke, Parkinson's, and dementia in their late 60's and early '70's. Who will look out for their well-being and security? Our retirees who invest their lives working for the state of Alaska deserve more.

The proposed legislation is particularly unfair to members of TRS who were pulled from Social Security, but not given the option PERS employees received when SBS was formed and the state matched the employee contribution of 6.13% . In addition PERS employees may participate in a

deferred comp plan. Teachers not only do not have a parallel SBS plan, they often receive little or no benefits under Social Security because of the provisions of the Government Pension Offset (spousal offset) and the Windfall Elimation Provision. These provisions eliminate or greatly reduce promised benefits from Social Security for quarters worked. Not only that, because the state mandates participation in Medicare Part B when a retiree reaches age 65, every retiree must pay almost $80 a month out of pocket for that coverage

Last year this Legislature unanimously passed a resolution requesting our Alaska Delegation in Congress work for the repeal of GPO/WEP. They recognized the inequities for public employees not covered by SS.

I urge you to give this matter more thought before you make sweeping changes. Let's work together for a year to get the health care costs down and look at some of the suggestions made by the Joint Boards at the presention of the Tier subcommittee's proposal in November. I am sure working together we can reach a solution that will be beneficial to future employees and also to Alaska's children. I want young people to come to Alaska and to stay in Alaska. We have much to offer. Thank you for this opportunity.

Steiman's comment – re: Bds – "we've had them all in here and all there's been is fingerpointing" I have never observed fingerpointing, only questioning of the actuaries information and I've been on TRS 6 yrs – this is the 1st time I've been allowed to come to testify. The other members can speak for themselves but to my knowledge, none have been down to testify since this process began + that includes a SBS. I testified yesterday that TRS PERS have great respect for ASRB's work and performance and for the time they spend managing retirees' funds.

Regarding testimony Mar 30. I was not called on, as listened to others

To: Senator Lyda Green, Chair, Senate Finance
From: Gayle Harbo, Teacher Retirement System Bd.
Re: Senator Stedman's Comments, Mar. 30 am, SFC

Senator Stedman, during his presentation on proposed Board reconfiguration, made a comment to which I take exception. Had I been allowed to give my testimony that day I would have responded in person, but realize the Committee had limited time that morning.

Senator Stedman, speaking in regard to the 3 retirement boards, said, "we've had them all in here and all there's been is finger pointing." I have never observed members of any of the three boards finger pointing. The Boards, in fact, requested an actuarial audit several years ago because they questioned some of the information they were receiving from Mercer. Milliman, the auditors, found several gross errors, particularly with respect for medical expense accounting. (see Sept. Joint Board minutes, page 6).

As I stated in my testimony on March 29, the three boards work well together and I have great respect for the members of ASPIB, the work they do and the staff which supports them. I don't know who Senator Stedman is referring to when he says "we've had them all in" - Mar. 29 is the first time in my 6 years on the TRS Board that I have testified and to my knowledge since SB141 came out no one on the three boards had testified before any committee. If he has names then tell us, but please do not make accusations.

Senator Stedman talks about professionalism on the Boards. The members we have now and have had are well respected members in their communities and give countless hours preparing for appeals and for other meetings, all on their own time. The Boards have always asked good questions and sought information from the actuary and Administration to make sound decisions.

I was dismayed at our last joint meeting that many of the Board members did not even receive the actuary's valuation until the day of the meeting. New information on how to calculate and project medical costs was contained in the valuation. For the first time health and prescription costs were separated and presented on cost per member basis, something I asked the actuaries for years ago. It makes it much easier to compare costs from year to year at a glance. Not only did we get new material, the Division had put a presentation on LTC on the agenda, which could have been held at a later time or scheduled for Fri., Mar.
25. These Boards are dedicated to serving members interests, another reason to have member representation. Employers are members of the system.
They too may be represented.

Thank for allowing me to testify on the 29th and I know my written testimony for the 30th is in the record.

Respectfully

Gayle Harbo

Retired Teacher
TRS Trustee

TESTIMONY by Gayle Harbo
TRS Trustee
House State Affairs and Senate Finance April 6, 2005

I know the legislature is trying to find solutions to a perceived problem with a retirement system that has worked well for almost 50 years. I respect your concern. I am not a political person, but I am an Alaskan of almost 50 years, a mother, a grandmother, a retired teacher and most recently a member of the TRS Board. I urge you to go slowly, get a second opinion from a credible actuary and talk with affected parties about the reasons for the decrease in the funding ratio before you impose devastating changes.

What affects the funding ratio? If you read the last valuation you will see that TRS is almost 92% funded without health care costs: PERS is 120% funded. Are these healthy systems???? What would your conclusion be? Has ASPIB done a great job??? What would your conclusion be?

Now look at the ratios with Medical costs factored in - remember Alaska is one of only 4 states that pre-funds medical costs. In FY'06, under GASB, all states will have to acknowledge medical costs as a liability. With Medical the TRS ratio drops to about 63% and PERS ratio to 73%. What would your conclusion be? What is the major factor affecting the declining ratio?

Medical costs have been the main factor and if the Administration would make some allowable changes, matters of choice and convenience, they could save millions of dollars on the health plan for the current tiers. They can change the Health Benefits for new hires without legislation - prospective is the key word here. Ask them why they have not made significant changes in the last 4 or 5 years.

You may have received a memo from Mercer, dated March 18, which shows two items which have also contributed to the unfunded liability. One is the enhancement of benefits that various legislatures have passed in recent years; some which the actuary said would be cost neutral. Actuaries, like airlines, are cautious people and always have a disclaimer, "subject to change without notice". They told you Retirement Incentive Programs would not negatively affect the funding ratio. This past year they changed their story - they did not predict the impact of medical costs correctly. The Boards asked for an Actuarial Audit in 2002 -2003 - In our Sept.'04 Joint Board minutes the auditor, Milliman, stated (on page 6) that Mercer 's "starting point for projecting forward was a number that was 14 percent too low." The minutes also reflect that medical costs account for 50% of the increases in employer contribution rates these past years. The Joint Boards, these past two years, have asked the Legislature not to pass legislation which will enhance benefits for existing Tiers and you have held off.



compliments of...
Gary Wilken

The second item in the March 18th letter refers to the Ad Hoc PRPA which is recommended by the Boards only when the fund is healthy. The sheet attributes huge costs to the Ad Hoc PRPA, but fails to mention that dollars of that cost was the settlement of a lawsuit that made all living retires whole, from their time of retirement, for ad hoc PRPA's that had not been awarded. Take that out and an ad hoc is a mere blip.

In the legislation proposing a DC plan teachers are more impacted than Public Employees. Teachers did not have the choice of an SBS plan when they were pulled from SS. Not only that, because they are public employees, even though they may earn SS credits, they will not get all that is due them because of two unfair Federal Provisions, GPO/WEP, which the Legislature last year recognized as unfair when they passed a resolution urging our Congressional Delegation to seek repeal.

I urge you to take time to get a second opinion. I urge you to work with the Boards and the Employers and the AML and successful Health Care Trusts and Plans to see how medical costs can be properly managed.

While I respect Dr.Solie's opinion, it is a lofty one. He may not realize that many of the people I worked with every day did not earn enough to save and invest the minimum needed to start a mutual fund. These people need the security and assurance in their senior years that a Defined Benefit offers. People need a system which recognizes inflation, as SS does, to adjust their annual retirement income.

Dr. Solie erred in his testimony on HB 238. He implied, using a 2000 mortality table and other assumptions used by mercer, that a person retiring from the proposed DC plan would be better off than a Tier I employee. It is a devastating error to future retirees, that I, a humble, public school teacher must point out. If this legislature did what Dr. Solie suggested many retirees would run out of dollars long before they died.

It is a grave error to apply group assumptions of a DB plan to individual assumptions on which DC plans are based. You would do grievous harm to thousands of seniors if you relied on Dr. Solie's data. Please go slowly and check and recheck and ask for all the information ... not selected sound bits.

Please work with the Boards these next years to solve the Medical cost problem, which is not unique to Alaska. We should be working together. The Legislature did not ask the opinions of the Boards before they introduced these bills. My late colleague, Bob Boko, a respected member of the Fairbanks Community, was not in favor of a Defined Contribution program. He knew it would be devastating to seniors. Though he chaired the Tier Committee and voted to recommend Option One of their proposed plan, he did so only because the Administration put pressure on him. After the vote in November, he wanted to meet and confer with the Joint Board members after our meeting with ASPIB on December 1st. He

wanted to discuss the suggestions we all had made. We were not allowed to meet. I urge you to speak with his widow, Sharon, who shares his deep concern.

Please let us work together to make Alaska a place where young people want to come and work. We can be a role model for health care reform if we choose to work together. I do not like the word "impose"; I prefer sitting down and discussing the problem and developing a solution which works for all. Thank you for your time.

April 6, Senate Finance

Testimony by Sam Harbo
UAF Retired Professor of Bio-Statistics

Longevity figures are estimates based on selected groups of individuals. Such estimates usually work well when used with projections associated with groups. such as the actuarial projections for the group of retirees in the DB plan. Individual retiree variations in such a plan (e.g. one retiree dying at an early age and another at an older age) tend to compensate for one another, with the actuarial projections accommodating continued pension payments to the long-lived retiree. Such is not the case in a DC plan. Everything there depends on an individual's history, not on group dynamics. Using group-based projections to evaluate a DC plan can hide a world of hurt.

For example, suppose the life expectancy is estimated to be 80 for the average retiree, with the amount of money (plus earnings) in a retiree's DC pension fund projected to last to year 80. Let us assume that all the underlying assumptions governing the above are objective and reasonable. Even if the above DC monthly pension payment is greater than what the retiree would have gotten under our current DB Tier 1 plan, one should not conclude immediately that the DC plan is better. At the very least, one should determine what proportion of retirees live to age 80, and what their life expectancy is at that age. Is it 6, 8, or 10 more years with no pension payment?

Another major difficulty with comparing DC and DB plans is that not all employees retire at the same age. That confuses the longevity picture (and any resulting projections) because an employee retiring at age 55 has a different projected mortality age than does an employee retiring at age 65. That is, life expectancy is retirement age specific. That difficulty is manageable in a DB plan because group dynamics are involved.
Unfortunately, group dynamics do not govern the fortunes of individual retirees in a DC plan; each individual's retirement age is paramount there.

I am not asserting that group projections are not useful in gaining insight into DC plans. In fact I have done just that myself. However, such projections must be evaluated and used with care. One must emphasize the individual in a DC plan.

Re: Boards Composition

Testimony SB 141
Gayle Harbo, April 2005 – Sent Apr 15 - Fbx delegation

The current system of 3 pension boards may , at first, seem cumbersome, but each has a slightly different role. The Boards work well together and the Jt Boards of TRS and PERS appreciate the time and effort of the Alaska State Pension Boards members to manage and invest the billions of dollars of pension fund assets. ASPIB's role and function was carefully crafted in the early '90's. They have done an excellent job and invested many volunteer hours.

PERS and TRS are advisory to the Administration, except for appeals, and in the case of PERS, setting the employer contribution rate.

It is important to have members of the system on any board which oversees the billions of dollars of pension fund money or listens to appeals. The boards are fiduciaries and should include members who contributed to the funds.It is also important for system members to have appeals heard and resolved by peers.

Elected representation from both TRS and PERS is a must on any board. I see no problem with merging the TRS/PERS Boards and I spoke at length with Rep Kelly's aide, Heath Hillyard, regarding the combination. A seven person board, with equal elected representation(for example 2 each as on the current PERS Board), plus one school district employer and one municipal employer and one other appointed person would be workable.

I ask you to please retain these important boards, keeping ASPIB with its current structure, and assuring there is elected representation of the parties who have contributed to the pension funds.

Gayle Harbo
Box 10201
Fairbanks 99710

Testimony of HB238/SB141
Gayle Harbo, April 2005

I have heard and read in the press that Alaska's public pension funds are in crisis. I have heard the figure " a 5 billion dollar unfunded liability". The liability is a crisis only if every PERS and TRS active member retires tomorrow and is paid all the money entitled to them for all their retired years. The funds, without health care costs, are in good shape. The earnings on the pension funds for each of the past two years have been 15% , better than the Permanent Fund. The funding ratios for non-medical benefits for TRS and PERS, based on market assets, are 93% and 120%, respectively. With medical benefits, the funding ratios drop to 64% and 74%, respectively. It doesn't take a rocket scientist to see that increasing health care costs are the problem. It is a recognized problem that can be solved without legislation. The Administration, working with employee groups, can make changes to current tier medical plans if the changes are for choice or convenience. They also have the ability to change the plan for future hires.

Have the funds been here before? You bet - in 1980, the funding ratio for TRS was 67%. At that time the contribution rate for the our model 50 year old system was roughly 7% each for employee, employer and the state, or 21% of payroll. When the state started funneling its share through the districts in FY'87, the contribution rate for the employer/state continued to decline to 12% until FY'05. The rate was then increased to 16%.Half the increase in the past few years has been caused by rising health care costs : a problem not unique to Alaska. This legislation seems to forget the state's share and speaks only to employee and employer sharing equally. No longer would 21% of payroll go to retirement.

Can the problem with health care costs be addressed? The Division of Retirement and Benefits and the Joint Boards of TRS and PERS have been working on cost containment, most recently with a generic drug campaign and in the near future with other measures such as preferred providers and closed formularies. The Division is also introducing a Positive Enrollment Program which they predict may save the state $16 milllion dollars.

So you ask, why is the problem called a crisis? Some interests, both in and out of Alaska, want to privatize public pension funds. Alaska is only one of several states where some legislators have " bought in" to the need to privatize the billions of dollars of such funds. Most Alaskans know that is not the path to follow - many past legislators like Jay Hammond, Terry Miller, Arlyss Sturgelewski and Charlie Parr worked to make Alaska's 50 year old retirement system a model for other systems in the country. Alaska is one of only four states which prefunds health care. Alaskans pride themselves on being independent and not having others tell them what to do.

The Employee Security Act which passed out of the senate as SB141 is a bill which assures ***no security*** for future retirees. It ***takes away*** the Defined Benefit plan which provides for a safe and secure income for Alaska's elderly in their golden years. In its

place is a DC plan. We all know DC plans discriminate against women, simply because they live longer. It would leave future retirees with no guaranteed monthly income, no health insurance and no cost of living adjustment. Many of these same legislators who would impose this system on future retirees have experienced what it means to take care of aging parents or loved ones who suffer from terminal illness or dementia, yet those same legislators would condemn future retirees to uncertain futures. It is not right, it is not fair, it is not necessary.

Talk with an employee who has been retired for 20 years or more and ask if they could now live on their base benefit, with no COLA or prpa. Under a DC plan there will be no incentive for retirees to remain in Alaska and contribute their time, expertise and pension dollars to Alaska's communities.

Why would our state, which has received almost 100% more than its budgeted amount for oil revenue, turn its back on seniors who have dedicated their lives serving Alaska's citizens? Only a few legislators would do this. They do not have the courage of those past legislators like Jay, Terry, Arlyss and Charlie. They do not have the courage of Senator Lisa Murkowski who has always been a strong proponent of public education and parent involvement. She had the courage to sign on to the repeal of the Government Pension Offset and the Windfall Elimination Provision, two provisions which reduce or eliminate Social Security retirement for thousands of Alaska's public servants. Senator Murkowski would not want to see legislation which would further discourage qualified teachers and public employees from coming to Alaska to work and from making Alaska their home.

Please ***"make Alaska proud"*** - contact your legislators , the Governor and our Congressional Delegation. Tell them we do not want outsiders tellling us how to run our pension funds. Our funds are in great shape if you look at the long term. As Michael O'Leary, the financial advisor for the Alaska State Pension Investment Board, recently said -"How powerful any time period is when looking at investment return". Think long term. Governor Murkowski, in his Dec. 13 2004 letter to seniors, stated "care for our elders and for vulnerable adults in our society is vital to our success as a state." He further states - ***"seniors should not have to choose between paying their rent, buying food or being able to fill prescriptions."*** That is exactly what many seniors will have to do if the legislature does away with a ***Defined Benefit*** retirement system. Please ask your legislators to ***"make Alaska proud"*** and retain our current ***Defined Benefit*** system. We can all work together to address health care costs.

We can work together to make Alaska a place where young people want to come and work. We can be a role model for health care reform if we choose to work together. I do not like the word "impose"; I prefer sitting down and developing a solution which works for all. There are many good things in this legislation which help close some of the loopholes, but doing away with a Defined Benefit plan is not one of them. Thanks for your time.

Gayle Harbo, Box 10201, Fairbanks 99710

April 18 2005

To: Governor Frank Murkowski
Capitol Building
Juneau, Alaska 99801 - 1182

From: Gayle Harbo
Box 10201
Fairbanks, Alaska 99710

Re: Retirement Legislation

Dear Governor Murkowski:

I know you are familiar with the myriad bills in the current legislature dealing with the retirement systems of PERS and TRS. Some legislators would make "Draconian" changes in our model, fifty year old system. These changes would give no immediate relief to employers responsible for past service costs, yet they would have a lasting, devastating affect on future hires. It has been pointed out to the legislators, over and over, that our system is quite healthy when medical costs are not considered. Alaska has always taken pride in our retirement system and the fact we are one of only four states which prefunds the medical benefits.

When the Tier Committee of the Joint Boards met, and worked for over year on a proposal to help contain costs, they presented many good ideas to close loopholes, to have a longer period of time to compute average salaries and to prevent people who are not career employees from vesting and accessing the health benefit component. They explored ways to reduce health care costs and to move the retirement age closer to the time when people would have access to Medicare, which at age 65, becomes primary to Alaska Care, our self-insured plan. No member of the Tier Committee supported a pure Defined Contribution plan, though a few supported a hybrid. Chair Bob Boko, a man of great integrity and honesty, was most upset when the Commissioner of Administration insisted that a pure DC plan be included. The Joint Boards, when presented with the final Tier Plan Nov. 19, could not support the plans presented because of the DC component. Board members had many helpful suggestions and wanted to meet again, at Mr. Boko's urging, after a meeting with ASPIB on December 1. They were not allowed to meet and tohave an open, honest exchange, nor the opportunity to reach consensus on a plan to which all could agree. The Boards did not want to be "a rubber stamp". The Tier Committee worked for over a year and one day was not enough time to be presented a plan and to be expected to make a well thought out decision when they were allowed little free discussion or time to point out the good points of the plan.

Governor Murkowski, we do not need to impose a Defined Contribution plan on future hires. The Employee Security Act, passed out of the senate as SB 141 is a bill

which assures ***no security*** for future retirees. It ***takes away*** the Defined Benefit plan which provides for a safe and secure income for Alaska's elderly in their golden years. It would leave future retirees with no guaranteed monthly income, no health insurance and no cost of living adjustment, which even Social Security provides. Furthermore, DC plans discriminate against women. Teachers are particularly vulnerable under the proposed plan, because when they were pulled from Social Security, they were not given the choice of an SBS plan as state workers were. They do not have that extra 6% contribution match provided state workers who in addition, have a deferred compensation plan. In your December 13, 2004 letter to Alaska's seniors you stated care for Alaska's seniors it is vital to the success of our state. You further stated - ***" seniors should not have to choose between paying their rent, buying food or being able to fill prescriptions."*** That is exactly what many seniors will have to do if the legislature does away with a ***Defined Benefit plan.***

I urge you to work with the Division of Retirement of Benefits to address health care costs. When Brenda Menge was Benefits Manager for the Division she suggested a HEALTH CARE FORUM, including employees, employers, unions, health care professionals and legislators to work on health care cost containment. We all know this is not a problem unique to Alaska. Alaska can be a role model for health care reform if we choose to work together.

I urge you to reexamine the states's obligation to our model retirement system. As, Sharon Boko, Bob's wife recently stated in comments to Representative John Holm, Fairbanks, "fifty years ago, when this retirement system was started, the employee, employer and state each contributed one-third, for a total of 21% of salary, to the retirement system. In the mid-80's the state funneled their share through the municipalities as revenue sharing. Three years ago, the state stopped this payment and have entirely abrogated their responsibility. The state has contributed greatly to the indebtedness problem - they now expect, under these new proposals, that employee and employer contribute equally , instead of meeting the original intent for each, state, employee and employer, to pay their fair one - third share."

Please encourage legislators to address the real problem, escalating health care costs. Please address it as a state and national problem. You and your daughter, Senator Lisa Murkowski, have been strong proponents of public education and parent involvement. You recognize the importance of attracting a stable quality workforce. - a workforce that will stay in Alaska and contribute to the community and economy, not a workforce that will take its money and run. As one retiree said to me the other day, under a DC plan there would be no incentive to remain in Alaska after retirement. We would lose a valuable resource - retirees contribute their time, expertise, and , yes, retirement pension dollars to each of Alaska's communities.

Please make Alaska proud and keep our Defined Benefit system, work on a model health cost savings initiative and keep Alaska a place where people, as we did, come to make their homes and raise their families. Thank you for your time.

YAHOO! MAIL Print - Close Window

From: "Cynthia L. Moore" <cmoorelaw@erols.com>

To: "NCTR Membership" <cmoorelaw@erols.com>

Subject: Victory! West Virginia Closes DC Plan to New Hires as of July 1, 2005

Date: Thu, 5 May 2005 16:22:07 -0400

Federal Update 2005-14

May 5, 2005

TO: NCTR Membership

FROM: Cindie Moore, Washington Counsel

RE: Victory! West Virginia Closes DC Plan to New Hires as of July 1, 2005

In a tremendous victory for defined benefit proponents, West Virginia has closed its teachers' defined contribution plan (the DC plan) to **new hires**. Anyone hired on or after July 1, 2005 joins the teachers' defined benefit plan (the DB plan). The total closure of the DC plan to **existing participants** may occur in the future. If the requisite number of participants so approve, the DC plan will merge into the DB plan in Spring 2006 and its participants will join the DB plan. If an insufficient number approve, the DC plan stays in existence. The provisions are part of HB 2984, a massive pension bill.

West Virginia closed its DB plan to anyone hired on or after July 1, 1991. Anyone hired on or after that date participates in the DC plan. West Virginia is the only state to create a mandatory statewide DC plan for teachers (although a very few statewide mandatory DC plans exist for other types of employees). In other states with DC plans, teachers (and other employees, if applicable) have the option whether to participate.

The key provisions of the bill follow:

- Closure of DC Plan to New Hires: The DC plan is closed to new members hired for the first time on or after July 1, 2005. The new hires become members of the DB plan. If a merger of the DB and DC plans takes place, all employees will become members of the DB plan effective July 1, 2006.

- Merger of DB and DC Plans: Existing DC plan members decide whether their plan should continue. If at least 50% of the members vote in favor of the merger during the election specified in HB 2984, the DC plan ends and the members go into the DB plan. If fewer than 50% approve, the DC plan continues.

- Education Program: The Consolidated Public Retirement Board (CPRB), which administers the DB plan, DC plan, and other plans in the state, must begin an educational program for existing DC plan members no later than August 1, 2005. The education program must include information such as the potential advantages and potential disadvantages of remaining in the DC plan or transferring to the DB plan.

- Election: The election may be held by certified mail and begins no later than March 1, 2006 and ends March 12, 2006. CPRB must certify the result to the Governor, Legislature, and DC plan members no later than April 5, 2006.

If you'd like to be removed from this mailing list, please contact me at cmoore@nctr.org.

MERCER
Human Resource Consulting

One Union Square
600 University Street, Suite 3200
Seattle, WA 98101-3137
206 808 8800 Fax 206 382 0627
www.mercerHR.com

March 18, 2005

Medical changes regarding HB 242 granted 5 yrs July '92 – '03

Frank '97 settlement – factored in medical emergence w/ note

Ms. Melanie Millhorn
Director of Retirement and Benefits
State of Alaska
Department of Administration
Division of Retirement and Benefits
P.O. Box 110203
Juneau, AK 99811-0203

Subject:
Changes in Funded Status – Plan Changes and Ad-Hoc PRPA's

Dear Melanie:

In previous correspondence we provided information regarding the factors that have affected the funded status of the Public Employees' and Teachers' Retirement Systems. Our January 3, 2005 letter analyzed changes in funded status from July 1, 1992 to June 30, 2003. During that time period, changes in plan benefits caused funded status to decline by 4.7% for PERS and 5.3% for TRS. Corresponding increases in the unfunded accrued liability were $0.3 billion for PERS and $0.2 billion for TRS. You requested we determine the effect of Ad-Hoc Post Retirement Pension Adjustments (Ad-Hoc PRPA's) compared to other changes in benefits.

	PERS		TRS	
	Change in Funded Status	**Increase in UAL (billions)**	**Change in Funded Status**	**Increase in UAL (billions)**
Change due to Ad-Hoc PRPA's	(3.7)%	$0.22	(5.1)%	$0.18
Change due to other benefit changes	(1.0)	0.08	(0.2)	0.02
Total	(4.7)%	$0.30	(5.3)%	$0.20

For both PERS and TRS, Ad-Hoc PRPA's were granted in 5 years during the period from July 1, 1992 through June 30, 2003. Other benefit changes were valued in 2001 and 2002 for PERS, and only in 2001 for TRS.

lawsuit settled in '96 or '97 accounted for most cost

How much from legis enhancements. 2B

17% of Payer

SB 2001 on Med. Base

WILLIAM M. MERCER

October 26, 2000

Mr. Guy Bell
Director of Retirement and Benefits
State of Alaska
Department of Administration
Division of Retirement and Benefits
P.O. Box 110203
Juneau, AK 99811-0203

Subject: PERS and TRS Surplus Assets

Dear Guy:

In our letter of August 23, 2000 we provided you with estimated costs for a number of proposed changes to PERS and TRS. These changes were initiated by the fact that there are funding surpluses in both Systems as of June 30, 1999. The Boards wanted to review ways of sharing some of these surpluses with members, through benefit improvements, and still maintain a fiscally responsible position with respect to the funding of the Systems and employer contribution rates.

At the August 30, 2000 Joint Board meeting these proposals were reviewed by the Boards and specific packages were recommended by each Board. As you may recall, each of the proposed changes was presented in isolation. We did not combine features of two or more of the proposals together in our original cost estimates. Now that the Boards have recommended specific packages of benefits we can evaluate the combination of changes to get a better estimate of the affect to System costs and funded status.

In addition, we have recently completed an analysis of actuarial assumptions for both Systems. Should the Boards adopt our ~~recommended~~ assumption changes, the funded ratio of both Systems will be reduced. It is possible that one or both Systems could have funded ratios of less than 100% as of June 30, 2000, i.e., there may be no surplus assets on an actuarial valuation basis.

While this possibility exists, evaluating the financial effect of surplus sharing is still applicable. As recent history with the Systems has shown, surpluses can accumulate in favorable market conditions in a relatively short period of time.

William M. Mercer, Incorporated
One Union Square, Suite 3200
600 University Street
Seattle, WA 98101-3137

Phone 206 808 8800
Fax 206 382 0627

WILLIAM M. MERCER

employee rate prop to employer rate

Another item that you have asked us to consider is setting the employee contribution rate proportionate to the average employer rate – a practice used in some other public sector plans. This method would increase (decrease) employee contribution rates along with employer rates and increase (decrease) the liabilities of the System with respect to the return of employee contributions. Taken as a whole and depending on design, it is not clear that there would be system savings or costs associated with this change. Because of this, we would like to discuss this further with you and the Boards before proceeding with any cost analysis.

We are available to answer any questions you may have concerning the above items.

Sincerely,

James W. Jacobson, ASA, MAAA

Brian R. McGee, FSA

JWJ/BRM/jls

g:\retire\akasea\#corresp\gb817new.doc

WILLIAM M.
MERCER

August 23, 2000

Mr. Guy Bell
Director of Retirement and Benefits
State of Alaska
Department of Administration
Division of Retirement and Benefits
P.O. Box 110203
Juneau, AK 99811-0203

Subject: PERS and TRS Surplus Assets

Dear Guy:

You have asked us to determine the actuarial impact to the Public Employees' Retirement System (PERS) and the Teachers' Retirement System (TRS) for certain benefit improvements. These improvements would decrease the surplus assets that have accumulated in both systems primarily due to recent investment gains.

Surplus assets for this purpose are defined as the excess of the valuation assets over accrued liability. The surplus in TRS was $94,679,000 at June 30, 1999. The surplus in PERS was $218,966,000, taking into consideration the PERS Board adopted target funding ratio of 102%.

The proposed changes are described below:

1. Creation of a "Cash Account" within the current system. Each active member is allocated a $500 initial account balance. Upon termination after vesting, the member is allowed to take this account balance amount, including a credit of 8.25% interest compounded annually (the current valuation interest rate assumption).

2. Full system-paid medical benefits for Tier II and Tier III members upon reaching 25 (30) years of service for Teachers and Police/Fire (Others).

3. Full system-paid medical benefits when vested and age 60 or older.

4. Full system-paid medical benefits for disabilitants upon reaching normal retirement.

5. A 13th check for current retirees equal to the members' monthly retirement benefit. The average TRS monthly retiree benefit is $2,388 and the average PERS monthly retiree benefit is $1,303 at June 30, 1999.

6. Automatic PRPA equal to full Anchorage CPI.

William M. Mercer, Incorporated
One Union Square, Suite 3200
600 University Street
Seattle, WA 98101-3137

Phone 206 808 8800
Fax 206 382 0627

	Current Assumption	Proposed Assumption	Change in: Calc. Funding Ratio	Change in: Contrib. Rate
Total Inflation	4%	3.5%	1.9%	(1.46%)
Annual Investment Return	8.25%	8.25%	No change	No change
Recognition of Asset Outside 5% Corridor	N/A	Adopt	No change	(3.21%)
Annual Salary Increase - Inflation Productivity Merit (first 5 years)	4.0% 0.5% 1.0%	3.5% 0.5% 1.5%	0.7%	(0.82%)
Health Premium Trend -	5.5% increase per annum. Blended monthly premium for FY00 is $459.33.	FY00 - 8.5% FY01 - 7.5% FY02 - 6.5% FY03 - 5.5% FY04-FY08 - 5.0% FY09-FY13 - 4.5% FY14 & later - 4.0% Blended monthly premium for FY00 is $486.00	(1.3%)	1.01%
Total Turnover Rates	See Table 4 on page 33.	See Table 1 on page 26. Patterns vary by age and service, but proposed rates are generally lower in the first eight years.	No change	0.22%
Disability Rates	See Table 5 on page 34.	No change	No change	No change
Retirement Rates	See Table 6 on page 35.	No change	No change	No change
Assumed Retirement Date if Under Age 50	After 22 years of service.	After 21 years of service.	(0.4%)	0.11%
Mortality Rates	1984 Unisex Pension Mortality Table set forward one year for males and set backward four years for females.	1994 Group Annuity Mortality Basic Table for males and females. 1994 Base Year.	(8.2%)	7.62%
Cost-of-Living Adjustment	62% of retirees receive COLA.	65% of retirees receive COLA.	No change	No change
Total Change due to Proposed Assumptions			(7.3%)	3.47%

Ginny Austerman

From: Ginny Austerman
Sent: Wednesday, July 13, 2005 10:17 AM
To: 'William Blackburn'
Subject: RE: PERS/ters hearing (includes typo corrections)

Thank you, William. I have given Rep. Weyhrauch a copy of this email.

Ginny

From: William Blackburn [mailto:webjno@gci.net]
Sent: Tuesday, July 12, 2005 7:49 PM
To: Ginny Austerman
Subject: Fw: PERS/ters hearing (includes typo corrections)

----- Original Message -----
From: William Blackburn
To: Ginny_Austerman@legis.state.ak.us
Sent: Tuesday, July 12, 2005 7:42 PM
Subject: PERS/ters hearing

I do hope that this hearing will address the shortcomings of the Administration that let to this situation of the fiscal shortages in the fund. Someone was not doing their job to let this get so out of hand. I cannot place further trust in the administration of our retirement fund until the misdeeds of the Retirement and Benefits are rectified, and the sooner the better. William E. Blackburn, 4143 Aspen St., Juneau,Alaska,99801. Please inclue this e mail as my testimony for the hearing in Anchorage, and get a copy to Rep> Weyhrauch. Thank you.

JUL 15 2005

Gary Miller
20135 Cohen Dr
Juneau, AK 99801-8211

Representative Bruce Weyhrauch
State Capitol Room
Juneau, AK 99801-1182

The $5.7 billion PERS trust fund shortfall is over a 25-year period. In other words it is $228 million per year. Part of the short fall was caused because the State reduced its payments by over $460 million. **The State needs to increase its payments.**

The State needs to stop hiring contract workers and retirees who come back to work. We had contract workers where I worked who we paid $150 to $200 per hour. **Pay overtime wages instead of hiring contractors.** Some money from the overtime wages would go into the retirement trust fund. Retirees who come back to work fill a position that then no longer contributes payments to the retirement trust fund. **Stop hiring retirees back.**

Both the State and state employees benefit from a good retirement system. The State benefits by making jobs more attractive. The State is currently in a crisis because of problems having trouble hiring new employees. A good retirement system helps both attract new employees and keep the trained and experienced employees. State employees benefit because they can look forward to a secure retirement after a career with the State**. State employees may need to contribute more to their retirement.**

Health care costs have risen several times the rate of inflation. There are several reasons for this that I am aware of.

Drug companies spend 13% for development but 30% for advertising. They are also spending huge amounts of money defending themselves in court. The people of the U.S. pay the highest cost for drugs in the world. Canadian drugs are much less expensive but President Bush and the drug companies are successfully keeping Alaskans from being able to buy drugs from Canada. **The solution is for the State to set up its own pharmacies and sell the drugs at cost to public employees and retirees.** There are 90,000 active and retired public employees.

Doctors pay huge insurance premiums for their malpractice insurance. In reality, we pay for the malpractice insurance through higher medical bills. If you watch the commercials on television you see attorneys drumming up lawsuits. **The solution is to limit how much money an attorney can receive per hour if they loose a case.** This will reduce the number of frivolous cases and should reduce malpractice insurance and thus healthcare costs.

The State offers free health care for the poor. Having health centers where nurses, not highly paid doctors, perform the assessments and checkups saves money. The patients are referred to doctors only when necessary. The same should be done for public employees and retirees**. State health centers staffed by nurse practitioners should be set up for active and retired public employees.**

Tobacco, alcohol, obesity etc. are all causes of increased healthcare costs. Approximately 26% of Americans smoke. Over 50% of Americans are overweight. Wellness programs may help people become and stay healthier, thus saving money. **Setup wellness programs for active and retired public employees.**

Annual physicals catch medical problems early and reduce the cost of treatment. I had a melanoma removed that had been discovered during my annual physical. Because it was found early I did not need chemotherapy or radiation. **Health insurance should cover one physical per year.** Dental cleaning is covered by insurance because it catches problems early and reduces dental costs. Annual physicals could do the same thing.

Please consider the above problems and solutions.

Thank you.

Gary Miller
Retired state employee

Gary Miller
20135 Cohen Dr
Juneau, AK 99801-8211

Representative Bruce Weyhrauch
State Capitol Room
Juneau, AK 99801-1182

I would like to add one comment to my previous suggestions. Factors affecting the PERS trust fund vary. Changes in the stock market, health care costs etc. affect the balance of the fund. Contributions to the fund are fixed. **The contribution rate for the employees and employers should vary based on actuarial projections.**

Thank you.

Gary Miller
Retired state employee

Gary Miller
20135 Cohen Dr
Juneau, AK 99801-8211

Representative Bruce Weyhrauch
State Capitol Room
Juneau, AK 99801-1182

I would like to add yet another comment to my previous suggestions. Since AETNA processes the medical claims, they make a profit that reduces the money available for claims. A study should be done to see if the State of Alaska could process the claims for less money than what AETNA charges. Even if the cost turns out to be the same, bringing the work from down South back to Alaska will create Alaskan jobs. **The State of Alaska may be able to process insurance claims for less money than what AETNA charges.**

Thank you.

Gary Miller
Retired state employee

Ginny Austerman

From: Bruce Weyhrauch [whyrock@gci.net]
Sent: Friday, July 15, 2005 4:04 PM
To: Ginny Austerman
Subject: FW: Pensions

file

From: David M. Reaume [mailto:dreaume@camano.net]
Sent: Thursday, July 14, 2005 3:31 PM
To: Bruce Weyhrauch
Subject: Pensions

Bruce:

I have been listening to the hearing today. As I write this Melanie Milhorn is testifying. My reaction is that fund valuation is being over emphasized. You really do not need another actuarial opinion to know that the funds are in trouble. Whether the shortfall is $ 5 billion or $ 10 billion is almost academic. Beyond a certain point, numbers are just "BIG." The focus now should be more balanced with a close look on how changes in the plans affect representative employees and pensioners. In other words, the macro problem is clear enough and the causes of the problem are clear enough. The issue now is how to fix it given budget constraints and how various proposed fixes affect not only the actuarial valuation but also the representative employee.

In particular, hiring a "health actuary" as suggested by Mr. Esuchanko is, in my opinion, an exercise with limited value because no one really knows how the country's health care crisis (continuous increases in spending) will turn out. Mercer's health care cost projections may be conservative as suggested by Mr Esuchanko but given the state's implicit budget constraints, knowing that the problem may be even more severe would likely have very little effect on the choice of solution. Knowing just how much more severe the health care problem may become is nice but not essential to the problem at hand because you probably could not pass legislation that dealt with shortfalls much greater than those projected by Mercer.

DMR

Ginny Austerman

From: Rep. Bruce Weyhrauch
Sent: Tuesday, July 19, 2005 9:28 AM
To: Bruce Weyhrauch
Cc: Ginny Austerman
Subject: FW: Alaska's aging population chart

From: Luby, John Patrick [mailto:JLuby@aarp.org]
Sent: Friday, July 15, 2005 12:41 PM
To: Rep. Bruce Weyhrauch; Rep. Mike Kelly; Rep. Max Gruenberg; Rep. Peggy Wilson; Rep. David Guttenberg; Rep. Ethan Berkowitz; Sen. Hollis French; Rep. Carl Moses; Rep. Norman Rokeberg; Rep. Paul Seaton; Rep. Ralph Samuels; Rep. Kurt Olson
Cc: Sam Trivett; barbara rich; Liz Lucas (E-mail); fjenkins@ak.org; George Hieronymus; Mary Schaeffer
Subject: Alaska's aging population chart

In yesterday's Ways and Means hearing, Representative Wilson asked about the percentages of older Alaskans compared to children after the comment about ten states with more older persons than kids.
Currently we have the smallest percentage of older persons in the entire country. Only 5.7 % of our population is over 65 compared to 12.4 % nationally. Alaskans traditionally are younger but we are seeing significant changes. We took the raw numbers produced by the Department of Labor and graphed them (see below). We definitely are going through a significant "graying" of our population. In addition, there has been a complete turn-around in the numbers of retirees who leave Alaska upon retirement. Only Nevada has a higher percentage of retirees who are determining to remain in their home state and not relocate. Before 1990, many Alaskans left. By 2000, that trend reversed and our folks are staying here after they retire.
AARP would be glad to secure any additional population info that may help you in your deliberations.

Ginny Austerman

From: John A. Lund [jalund@gci.net]
Sent: Friday, July 15, 2005 12:13 PM
To: Ginny Austerman
Cc: Rep. Ralph Samuels
Subject: Re: TRS/PERS

Open letter to the House Ways and Means Committee:

Good Morning. Will anybody be testifying as to how much the early buyouts (RIP programs) cost the retirement systems? Or how much medical costs were incurred by the system from members that where allowed to retire early ? (with TRS it would be three years,and during those three years are there any figures as to major medical costs that would have been the responsibility of the school districts but now are the retirement systems...i.e. cancer, bone marrow transplants)

It is one task to evaluate the general health of the system, it is another to assess the added costs brought about by the changes (loopholes) to the system. And how those changes effected the fiscal and actuarial health of the system.

How would the systems fiscal health be if we had no early buyouts, and part time employees were not given full time lifetime health insurance ?

The question is for the committee is, was it the perfect storm of high medical costs, increased life expectancy, and stock market losses, or was it government creating additions to the system that drained its fiscal stability ? The state funding public services through the retirement system.....i.e. the retire/rehire program, granting half time legislator's full time health benefits ?

Or why major unions in the state did not cry out to have the retire/rehire program revoked ?

Any figures on retired/rehired individuals having major medical operations during the period they were on retired/rehired status ?
(i.e. the retirement system rather than the retire/rehire employer picked up the costs)

Please have testimony on the "additions" to the system which created stress to the retirement systems fiscal health.

Yes, we have a contract with the state employees. Do we have a contract with the loopholes that were created ?

Also, I have been told that a preferred hospital (not providers) and generic drugs would greatly decrease raising health costs.
Why is that not being addressed ? Members could go to a non preferred hospital and use brand named drugs but that additional cost would be their responsibility.

The permanent fund always had Rick Halford and Jay Hammond to protect it's fiscal health. Sadly, the retirement systems' had no protectors. Greed and lack of oversight ruled the day.

Please submit this for the record. I would be available for testimony if asked.

Thanks

John Lund

Ginny Austerman

From: John A. Lund [jalund@gci.net]
Sent: Saturday, July 16, 2005 1:32 AM
To: Ginny Austerman; Sen. Ben Stevens; Rep. Mike Hawker
Cc: Rep. Ralph Samuels; Rep. Max Gruenberg
Subject: Fw: Article

Please add this to the mix. I knew when I wrote this I would be criticized. I'm protecing the person who sent this to me which is only fair. However the dialogue needs to be elevated.....jl

Good to hear from you. My only point is there was a rush to access the resources of the retirement systems. I don't believe there was enough due diligence or caution before accepting what the actuaries said. Was there any second opinion by other firms ? The actuaries were taken at face value because that is what folks at that time wanted to hear. Everyone wanted an early out. And in the end, that was beginning of the decline of a once great system.

The system questioned investment presentations and systematically invested wisely. Why was this not done with the actuaries ?
The answer is simple, too many folks wanted their districts to participate in the RIP programs and the consequences to the system were overlooked.

I know many will disagree with me. The system can work if it is allowed to stay actuarially intact and not tampered with by the legislature or special interest groups.

I hope all is well in your world. Thanks for the reply.

John

> John,
>
> When the retire/rehire bill was in the legislature a few years ago, we (-Alaska) raised questions about how it would impact the system. The response from the actuaries hired by the division of retirement and benfits was that ther'd be no impact.

Terry Harvey

From: Ginny Austerman
Sent: Monday, August 01, 2005 2:46 PM
To: Terry Harvey
Subject: FW: Quick Follow up

Thanks, John. I'll add this to your other comments.

Ginny

From: John A. Lund [mailto:jalund@gci.net]
Sent: Thursday, July 28, 2005 9:37 PM
To: Ginny Austerman; Rep. Max Gruenberg; Rep. Mike Hawker; Rep. Ralph Samuels
Subject: Quick Follow up

Good evening. My only point is after 25 years of a record bull market in equities, we will see a period of restrained growth. And higher energy prices, and the costs for terrorist protection, will take time to show a gradual raise in inflation.

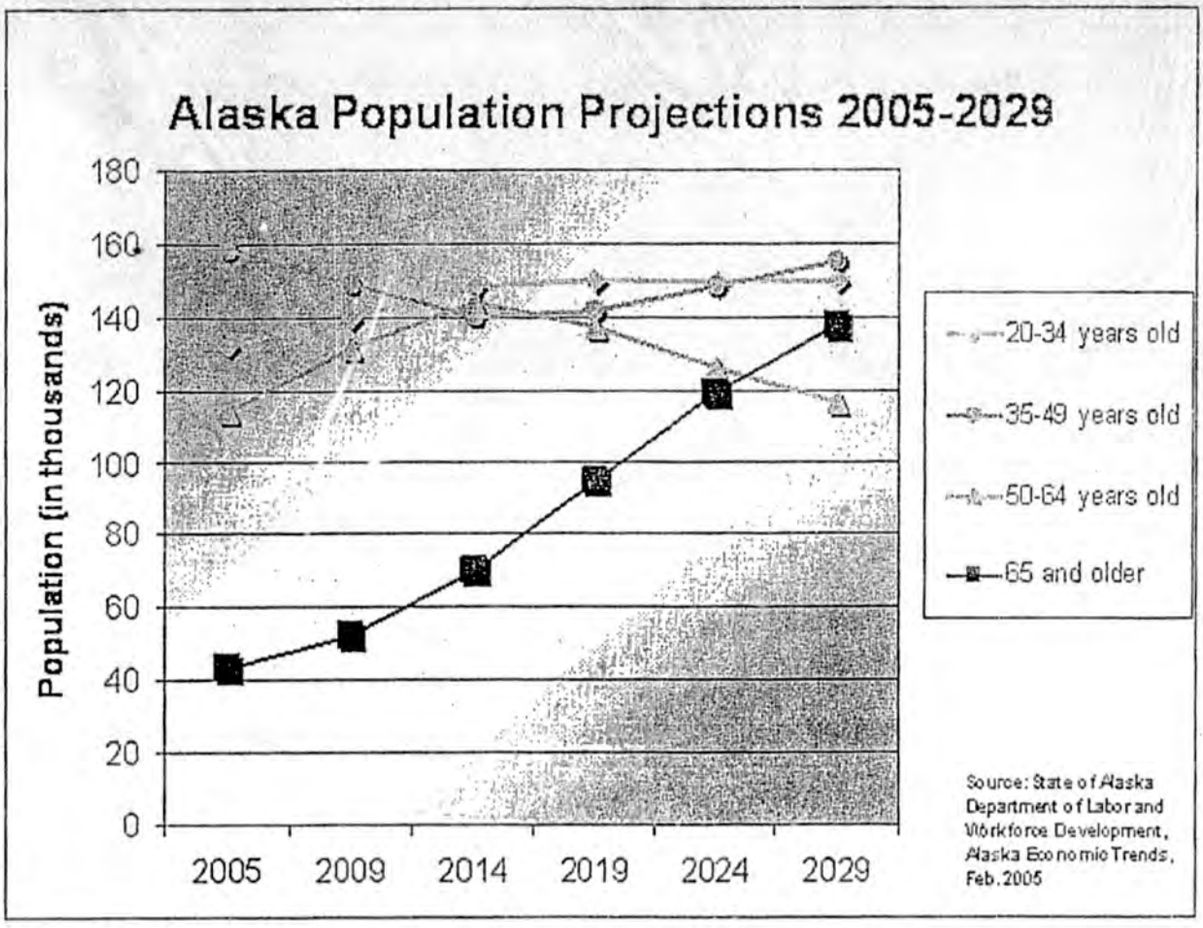
And the outside factors of possible terrorist attacks or disruptions, and the pending pension crisis in our country, added to a possible real estate bubble, would encourage me to go conservative on my estimates for stock market appreciation and continued low inflation.

If correct you have hedged your bets and can further reduce the unfunded liabilities, if wrong you have increased the unfunded liability and compounded the problem.

My rule of thumb would be always go a half a percent of what the permanent fund projects for capital appreciation and read their inflation outlook.

I appreciate all you are doing.

John Lund



Alaska's aged population is expanding.

In 2003, Alaska's population was about 649,000, with 6.3% being age 65 and older (41,000 residents).[1] Unlike any other age group, Alaskans age 65+ is currently growing at three percent annually. Comparatively, the growth rate for *all other age groups* is just 1%.[2]

[1] OASDI Beneficiaries by State and County, 2003. Social Security Administration: http://www.ssa.gov/policy/docs/statcomps/oasdi_sc/2003/table1.html

[2] Alaska Economic Trends Population Projections 2005-2029, State of Alaska Department of Labor and Workforce Development. http://www.labor.state.ak.us/trends/feb05.pdf

Patrick Luby
AARP Advocacy Director
3601 C Street, Suite 1420
Anchorage, AK 99503
907-762-3314
907-599-0839 (cell)
jluby@aarp.org

Doris Robbins
3763 Mitchell Avenue B
Fairbanks AK 99709-4636

(907) 374-0597
drobbins@gci.net

8/24/2005

Representative Bruce Weyhrauch
House Ways and Means
State Capitol, Room 421
Juneau, AK 99801-1182

RE: PERS/TRS Funding Shortfall

I speak for myself in this writing, but as a PERS/TRS retiree, I am an active member of the Retired Public Employees of Alaska (RPEA). Through that organization, I have had an opportunity to communicate with many PERS and TRS retirees. My impression is that there is a general feeling that retired State of Alaska employees have received unfair treatment at the hands of those we elected to represent us. On reviewing the actions of the legislature last session, it appears to me that nothing has been done for retirees, and the only fix "for" new employees has been to cut benefits. The subject of this hearing is on the retiree funding shortfall, so I will stick to that.

When I was working for the State of Alaska, not once was I allowed to be involved in the decision making on my contribution rate or any issue related to how much would be set aside from me or by my employer for my retirement benefit. I did give up wage increases a number of times because the state was going through a rough patch. With that I was promised all along that my health benefits would remain at the same level as promised when I was hired. Instead, there is the constant threat of another diminishment of benefits around the corner.

Now, retirees are being asked to accept less than promised. We are being told that the shortfall is our fault, or the fault of the retirement boards upon which we had some representation. No one talks about the fact that the administration has always had final say over the boards, and that laws governing retirement issues were all passed by vote in the legislature. No one mentions that boards upon which retirees had representation questioned too rosy actuarial reports, and those questions and recommendations were unheeded by administration officials.

Therefore, it is up to the administration and the legislature to fix the shortfall. Begin by using common sense actuarial methods similar to those of almost every state in the Union except Alaska. Use realistic funding levels, again like most other states use. Pay off the under funding over time, by some legislative methods that you were

elected to figure out. It is the legislature's and the governor's responsibility to make sound decisions in every area of state government. This case is no different. The sooner the legislature begins work on the actual problem, instead of placing blame on everything except the sources of the problem, the faster the red ink will begin to disappear.

In addition, allowing retirees to participate in solutions, as in the case of the PERS and TRS boards, you might find more savings to be had. As a result of past cooperation, we now have about the highest possible savings from using generic prescription drugs that is possible until some newer brands become generic. I and others in my circle are worried that lack of oversight with the new ARM board will result in the escalated erosion of our retirement funds. Please take positive action to fix the increasing funding problem.

I thank each of you who are involved in looking for solutions. You are giving additional time to solving problems that should not have remained on your plate at such a late date. I truly appreciate your service to the people of Alaska.

Sincerely,

Doris Robbins

cc:

Representative Rokeberg
Representative Samuels
Representative Seaton
Representative Wilson
Representative Gruenberg
Representative Moses

Ginny Austerman

From: Rep. Bruce Weyhrauch
Sent: Monday, July 11, 2005 2:20 PM
To: Bruce Weyhrauch
Cc: Ginny Austerman
Subject: FW: TRS

From: John A. Lund [mailto:jalund@gci.net]
Sent: Monday, July 11, 2005 12:54 PM
To: Rep. Bruce Weyhrauch
Subject: TRS

VITAL SIGNS

Employers' differing stances on health
Unions, profitability, industry affect coverage decisions

By Kristen Gerencher, MarketWatch
Last Update: 7:22 PM ET July 7, 2005

SAN FRANCISCO (MarketWatch) -- When it comes to providing health care for their workers, companies vary widely in how they perceive costs and value.

At one end of the spectrum are the companies that pay 100% of the health premiums for their employees and seek to hold down costs in the health plans themselves. On the other end are firms that ask workers to pick up a bigger percentage of the tab and implement high-deductible plans that pin more of the health-care decision-making on employees as well.

With health-care costs continuing their rapid rise, just what persuades one company to absorb most of the cost increases while another passes the hikes on to workers or scales back coverage?

"The way a company looks at that question is going to be shaped by what industry they're in, what their cost pressures are, what their competitor does, how profitable they are," said Tom Billet, senior consultant for Watson Wyatt, a benefits consultant in Stamford, Conn. "Those are all key factors.

"Beyond that... I would say there's one constant in today's environment and that is very few companies if any that feel they have to have a top-of-the-line plan to attract and retain employees. More companies look at it as they want to make sure they have a competitive plan."

The kind of coverage a company offers and the amount of the tab it picks up depends on variables ranging from labor relations to profitability to executives' personal

beliefs, benefits experts said.

Such factors make the experience at General Motors or Starbucks, for example, vastly different from that of other employers.

Holding on to top benefits

The strength of unions, despite a decline in recent years, remains instrumental in some sectors.

General Motors (GM: news, chart, profile) is embroiled in a long battle to enlist union support in getting its medical costs under control as it now spends more on current and former workers' health care than it does on steel.

The automaker's woes are more extreme than those of many other companies because it hasn't yet successfully bargained to participate in employee cost-sharing, the dominant cost-control strategy that emerged after consumers rejected tightly managed care in the 1990s, said Paul Ginsburg, president of the Center for Studying Health System Change.

"The auto companies always had the richest health benefits," Ginsburg said. "Some other unions have made concessions recognizing it was coming out of wages and they had some interest in containing health-care costs."

Part of GM's dilemma is that "it's usually harder to take something away that exists," said Ron Pollack, executive director of Families USA, a consumer advocacy group.

"There are some industries and some companies where it may be harder to take back just because of how much a tradition this has become in terms of the coverage they've had for many years," Pollack said.

Star-bucking the trend

Despite the cost pressures, some executives have taken a strong position, Pollack said. "[Chairman Howard] Schultz at Starbucks is proud that he provides significant coverage for his workers. There are some companies and some industries where that's more prevalent than others."

For 20 years, Starbucks (SBUX: news, chart, profile) has provided health care for all eligible workers, including part-time staff who work about 20 hours a week, spokeswoman Sanja Gould said. "We have created PPO plans designed to provide coverage that is affordable to all partners while providing comprehensive coverage."

The vast majority of workers who participate enroll in one of two PPO plans that have deductibles ranging from $100 to $225, she said. Starbucks covers about 75% of the premium costs while workers pick up 25%, and the company currently has no plans to change its offerings for next year.

"The health benefit is a key component of the Starbucks business model," Gould

said. "By providing a health benefit, Starbucks is able to reduce partner turnover, attract higher quality applicants and ultimately foster a more fulfilled, productive and healthy partner in the short and long term."

Playing defense

Starbucks is unusual in the retail sector, which isn't known for many, if any, health benefits. Wal-Mart, for instance, has come under fire for having a large share of its workers enroll in public health-care programs, putting taxpayers on the hook for benefits critics say the company should offer.

Wal-Mart (WMT: news, chart, profile) spokesman Dan Fogleman said the company tries to make its plan affordable for workers, whose national average hourly wage is $9.68. The company's self-insured traditional 80-20 plan offers eight options, with deductibles ranging from $350 to $1,000 a year, he said.

"A lot of people don't realize we offer benefits to both full and part-time associates, which sets us apart within the retail industry," he said.

Wal-Mart, which Fogleman said has thin profit margins, picks up about two-thirds of the premium costs and "associates" carry about one-third. Single workers can get insurance for less than $40 a month and family premiums typically run $155, he said.

While plans for 2006 are still being considered, "we are very interested in and are looking at adding HSAs to our offerings," he said, referring to health savings accounts, which are new worker-owned, high-deductible plans that function like tax-free investment accounts for offsetting health expenses.

Some companies take great pains to shield their workers from health-care costs.

Analytical Graphics in Exton, Pa., was one of 20 firms making the list of 50 "Best Small and Medium Companies to Work For" that covers 100% of workers' health premiums. Only 14 of Fortune's "100 Best Companies to Work For" cover that much of their workers' health care, according to the Great Place to Work Institute. See full story.

Still, premium costs are just one measure of a company's approach to health care, Billet said.

"Just because a company doesn't have payroll contributions doesn't mean it has a great plan," he said. "They might have very high cost-sharing in the plan itself."

The most prevalent arrangement at big companies is for the employer to shoulder 80% of the cost increases while workers take on 20%, though that split is shifting toward 75-25, Billet said.

Lisa Velte, director of human resources for Analytical Graphics, said the point-of-service plan that has no premium cost to employees is one of four plans the company offers. It's considering replacing one of its other PPO or HMO offerings with an HSA next year, she said, noting that there aren't a lot of HSA options on the market yet.

The software firm's 240 workers are fairly young and healthy -- 37 is the average age -- and that may help the company get a handle on its 11% projected health-care cost increase for 2005-06.

"We try to structure the plan as best we can to control the costs," Velte said. "It's the fastest growing part of our employee investment, but it hasn't been as bad as the rest of the industry."

"We also know that making this investment in our employees is extremely valuable," she added. "It's a retention and attraction tool."

To be sure, privately held firms may find it easier to offer generous medical benefits because they don't have to answer to shareholders as do their publicly traded counterparts, and large companies that self-insure can make comparisons difficult, said Billet, of Watson Wyatt.

In fact, more small firms have stopped offering coverage altogether in the last few years, with just 63% providing it last year compared with 68% in 2001, according to the Kaiser Family Foundation. The percentage of all workers getting employer-sponsored care fell to 61% from 65%.

Kristen Gerencher is a reporter for MarketWatch in San Francisco.

Bruce,

I thought you would find this interesting.....

John Lund

Ginny Austerman

From: John A. Lund [jalund@gci.net]
Sent: Thursday, July 28, 2005 12:07 PM
To: Ginny Austerman; Rep. Max Gruenberg; Rep. Mike Hawker
Cc: Rep. Ralph Samuels
Subject: TRS

Good Morning. Just can't get out of this print. Two points, one, inflation will probalby be up, and two, you can't expect high upper digit returns. To me, inflation will be higher than 2.6% and a 6.5% return on investments is more realistic.

I have enclosed two articles to look at.

John Lund

Mercer's Assumptions	Alaska's Experience
Inflation will be 3.5%	2.6% over any ten year period; PF uses 3%.
Wage Growth 3.75-4.5%	1.36%
Investment return 8.25%	9% over any ten-year period
Health Care Costs 12.5% - 5%	8% (7.5% according to Esuchanko)

The Street.com
What's ahead as China revalues the yuan
By Tony Crescenzi 7/28/2005

China's revaluation of its currency, the yuan, has varied implications. Here I'll present several of them along with other key points and facts and figures on the issue.

The Treasury market's initial reaction was overdone, as China's monthly purchases of Treasurys are not likely to change much anytime soon. The revalue isn't likely to result in more than $1 billion in monthly impact at most, and this is a stretch. With Treasurys trading nearly $600 billion per day, such a sum would be a drop in the bucket.

The $1 billion maximum forecast is derived by considering that China has been purchasing about $2.3 billion of coupon Treasurys monthly over the past year, in addition to about

advertisement

$1.8 billion of T-bills. Thus, China's total monthly purchases of Treasurys have averaged about $4 billion per month. It seems unlikely that the modest yuan revaluation would alter the monthly tally by more than several hundred million dollars per month.

Start investing with $100. Explore our new ETF center.

Moreover, even with full flexibility, China is likely to continue to accumulate Treasurys, just as Japan has been a large buyer for many years despite having a fully flexible foreign exchange system. The main reason is because China, like Japan, earns large amounts of dollar reserves on a daily basis. Many of these dollars will flow back into the Treasury market.

What it means for inflation

The impact on inflation will be minimal. For each 1% rally in the yuan, import prices will rise by about 0.14%, given that China accounts for about 14% of all U.S. imports. The impact is actually likely to be smaller than that, assuming substitution effects and the fact that some of the U.S.-China trade is being conducted in dollars. A 10% revalue would thus boost import prices by about 1.4%. The impact on U.S. consumer prices would be diminished by the fact that the $215 billion in annual imports from China are a very small part of the $12 trillion U.S. economy. It would thus take a 5% revaluation of the yuan to move the consumer price index 0.1%, again assuming no substitution effects (unlikely) and the false assumption that all of the trade between the U.S. and China is transacted in yuan.

Related news and commentary on MSN Money



- China: the dragon that isn't
- China scraps currency's peg to the dollar
- What China needs now: unions
- Own a piece of China's Google wannabe
- 12 ways to invest in China's boom
- Prepare for the global money crunch

For those who worry that China will sell some of its Treasury holdings when it begins to diversify its reserve assets, it should be noted that Japan, which holds $685 billion of Treasurys, has been diversifying its reserve assets since August and has hence been a net seller of Treasurys, yet interest rates have nonetheless fallen for the most part since then. In the same way, if China were to diversify its assets, the impact would likewise be minimal and readily absorbed, especially with the U.S. budget deficit on the way down, which is freeing up tens of billions of investment dollars.

China's impact on the U.S. fixed-income market extends beyond Treasurys. Over the past year, China bought about $19 billion of U.S. corporate bonds and $17.2 billion of agency securities. Here too, however, the sums are too small to impact the main dynamics shaping these markets. Nevertheless, to the extent that the corporate and agency markets are smaller markets than the U.S. Treasury market, the impact could be greater, albeit small.

The rest of the story

There is a secular story here related to labor costs and inflation that may be bearish for the bond market but which will take many years to play out. China's revaluation symbolizes its emergence as an economic power and its increased status, and this should benefit Chinese households by boosting incomes there. As China's labor costs rise, the disinflationary effects from China that have helped keep global inflation low over recent years will wane, thus boosting inflation. Nevertheless, with labor costs at roughly 30 cents per hour in much of China, it will be many years before Chinese labor costs are high enough to provide much of an upward thrust to global

inflation.

Future moves toward flexibility of the yuan are likely to coincide with China's economic news. It is no coincidence, for example, that China announced its revaluation just a few days after it reported strong GDP data. The timing of the announcement was likely a signal about what would likely be a catalyst to future revaluations. China's fixed-exchange-rate regime has been a source of economic strength because it has invited the inflow of foreign capital. It's akin to **eBay** (EBAY, news, msgs) keeping its stock price at $80 while its value has actually increased to $300+. If such a situation existed, investors would pour money into eBay, recognizing the cheapness of its shares. Similarly, the fixed regime in China has made China a cheap investment, and money has poured in. This creates the risk of imbalances such as excess capacity, something that revaluations will help to avoid.

China likely wants to keep its currency somewhat overvalued to allow for a cushion against weakness when economic growth eventually slows and hence the veritable exit from one door commences.

China is unlikely to move toward a fully-flexible exchange rate for at least several years, as China will want to protect its economic gains via the relative stability of the U.S. dollar. China is already hinting as much, judging by comments that Li Deshui, a member of the Bank of China's monetary committee, delivered in an interview with Bloomberg. He said it would be at least five years before China moved toward full convertibility of the yuan because if it were done sooner, there would be a risk of speculation against the currency, as was seen against the Korean won and the Thai baht in 1997. Such speculation would be possible if China's economic growth was to slow and its banking sector's woes were hence put under greater scrutiny.

Yuan Revaluation
• The impact of China's yuan revaluation will be felt far and wide.
• China is likely to keep accumulating U.S. Treasurys because it earns large amounts of dollar reserves on a daily basis.
• China is unlikely to move toward a fully-flexible exchange rate for at least several years.

The speed of future yuan revaluations will be dictated in part by the actions of the Federal Reserve and the impact that the Fed's actions have on the value of the U.S. dollar. For example, if the Fed were to cut interest rates, hence creating a downward tendency for the dollar, the Chinese might speed the pace of future revaluations, as it would fit naturally with the fact that other currencies are rising faster against the dollar, too. Conversely, when the Fed raises interest rates and the dollar rallies, the Chinese are likely to slow the pace of revaluation, as it would fit with the fact that the dollar is rising in value against other currencies.

Tony Crescenzi is the chief bond market strategist at Miller Tabak + Co., LLC, and advises many of the nation's top institutional investors on issues related to the bond market, the economy and other macro-related issues. At the request of the Federal Reserve, Crescenzi is a regular participant in the board's Livingston Survey of economic forecasters. He is also the author of "The Strategic Bond Investor." At the time of publication, Crescenzi or Miller Tabak had no positions in the securities mentioned in this column, although holdings can change at any time. Under no circumstances does the information in this column represent a recommendation to buy or sell stocks. Crescenzi also is the founder of Bondtalk.com, a popular Web site covering the bond market and the economy.

© 2005 TheStreet.com, All Rights Reserved.

Stock-Market Returns May Not Meet Bush's Social Security Hopes

March 28 (Bloomberg) -- President George W. Bush, promoting his plan to set up private Social Security accounts, is betting that stock returns will remain strong even as economic growth slows. Economists and equity strategists aren't so sure.

Bush is using forecasts from the Social Security Administration that say the economy will expand less than 2 percent a year -- the slowest sustained rate since the 1930s -- after 2020 as population growth eases. At the same time, the agency projects that stocks will return an annual average of 6.5 percent after inflation.

Thirty-nine of 58 economists and strategists surveyed by Bloomberg News say that if the economy slows that much, Bush's stock outlook is too optimistic. Over the last 50 years, as the U.S. economy grew 3.4 percent a year on average, almost twice as much as the agency is forecasting, the Standard & Poor's 500 Stock Index returned only 6.8 percent after dividends were reinvested.

``A 6.5 percent real equity return is not realistic'' at the growth rates being projected, says Thomas McManus, chief investment strategist in New York at Banc of America Securities LLC. ``If it were, we will not have a Social Security problem in 2050 because shareholders will be so wealthy they could easily fund the shortfall.''

Neal Soss, managing director and chief economist at Credit Suisse First Boston Inc. in New York, says that ``real growth of 1.9% and real stock market returns of 6.5% can go together for a significant stretch of time, but not in perpetuity. Among other things, that combination would suggest that eventually all of national income was being paid as profits with no wages at all, or alternatively that price-earnings multiples were rising without limit.''

`Way Too Low'

If the economy grows faster, the problems with Social Security won't require the overhaul Bush is proposing, several economists say.

``These GDP estimates are way too low, even with a slowing workforce due to retirees,'' says Chris Rupkey, senior financial economist at Bank of Tokyo-Mitsubishi in New York. ``With GDP faster than their assumption, there will be more money in the trust fund, or we will have paid down some debt with potential budget surpluses so we can borrow again to get through the baby- boom retirement period.''

The possibility of low stock-market returns could undercut the main arguments that Bush, Vice President Dick Cheney and Treasury Secretary John Snow are using as they try to convince the public that personal accounts invested in equity and bond index funds can result in bigger benefits for future retirees.

Exhausted of Assets

The Social Security trustees said on March 23 that the 70- year-old program will be exhausted of assets by 2041. The White House is using such forecasts to bolster its case that workers should be allowed to divert payroll taxes into higher-yielding private accounts.

Under the current system, Social Security funds are invested in Treasury bonds. The Social Security trustees project a 3 percent long-term return for the bonds, and Bush says the stock and bond markets will do better.

``The point is, the individual would get a higher rate of return than if they just send their money to Social Security,'' Cheney told an audience in Bakersfield, California, on March 21.

Economists such as Robert Shiller of Yale University say counting on averages from the

past to predict returns decades from now is dangerous. ``These historical returns are not, however, a good guide to future returns,'' Shiller said in a research paper released last week.

A Lucky Experience?

``The United States economy and stock market performed extremely well over the last century,'' he wrote. ``Many factors suggest this lucky experience is not likely to be repeated.''

He cited forecasts for lower economic growth and the current historically high stock values. The price-earnings ratio for the Standard & Poor's 500 index from 1936 through 1990 was 13.2 on average; it rose to an average 24.8 from 1991 through 2003, according to S&P data. The ratio was 19.6 as of March 24.

Shiller wrote the 2000 book ``Irrational Exuberance,'' which chronicles the 1990s stock boom and the phrase Federal Reserve Chairman Alan Greenspan made famous in a 1996 speech warning about a possible bubble in the equity market.

The White House Council of Economic Advisers said in a Feb. 4 statement that investment returns don't necessarily have any relation to economic growth. Greenspan echoed that view in testimony before the Senate Committee on Aging on March 15, saying that stock prices are closely related to investors' expectations of future earnings, reflected in price-earnings ratios, not just economic growth.

Slower Profit Growth

``It is the case if you have a slower economy that profits will grow at a slower rate,'' Greenspan said. ``But remember, a very significant part as far as equities is concerned is the price-earnings ratio.''

He added, ``It's ambiguous as to what that will do over time. And I wish we could forecast that better, but we don't seem to do that all that well.''

A Bloomberg analysis shows a strong correlation between investment returns and economic growth over the last 50 years. Gains and declines in the S&P 500 index preceded corresponding gains in gross domestic product and losses by about a year. The correlation coefficient was 0.92, with 1 being a perfect correlation.

Greenspan said workers close to retirement shouldn't be exposed to risk and should be largely invested in bonds. Bush and the Social Security Administration are also recommending that workers hedge their risk. They're touting a ``lifecycle portfolio,'' where older workers invest more in bonds than stocks.

Lifecycle Returns

Lifecycle-account returns may be even less than the 3 percent annual yields that the Social Security Administration forecasts for Treasury bonds over 75 years. Shiller analyzed 91 different scenarios for a worker born in 1990, and the median return was 2.6 percent.

McManus and 46 of the other 57 economists and strategists polled said the Social Security Administration's economic-growth forecast was too low, and that higher growth would yield better returns on stocks. Twenty of those surveyed said stock market returns would likely match or exceed the historic average.

If their prediction is true, it tempers the urgency to overhaul the federal retirement program, as higher economic growth results in increased wages and more workers, with more tax revenue going into the pension system.

``This low estimate ignores the potentials for immigration growth, an increase in the retirement age and significant productivity growth stemming from technology enhancements,'' says Ernest Goss, an economist at Creighton University in Omaha, Nebraska, and former scholar-in-residence at the Congressional Budget Office.

Productivity

Treasury's Snow says high stock-market returns will be possible because gains in productivity -- or output per worker -- will continue to be strong, offsetting slowing population growth.

GDP growth is a function of both growth in the workforce and productivity, he said in a March 23 interview. ``Productivity stays strong, and productivity per capita remains high,'' predicted Snow, who has a Ph.D. in economics. ``And it's productivity per capita that drives returns on assets.''

Yet the Social Security Administration expects productivity growth to plummet in the coming years, falling from last year's 4.1 percent gain to about 2.1 percent starting in 2010, according to the agency trustees' report released March 23.

Better Solution

Many economists who say Bush's forecast for investment returns is unrealistic still say private accounts are a better solution than the current system of paying for retirement as the baby boom generation -- those born between 1946 and 1964 --leaves the workforce.

``The money has to come from somewhere,'' says Stephen Stanley, chief economist at RBC Greenwich Capital in Greenwich, Connecticut, who was also included in the survey. ``Under the current system, we save nothing, which means we are on the hook for all the necessary payments in the future. Under personal accounts, people are saving a part of their eventual retirement income. Whether investment returns and the economy are good or poor, the burden will be spread out over time.''

To contact the reporters on this story:
Alison Fitzgerald in Washington at afitzgerald2@bloomberg.net
Michael Forsythe in Washington at mforsythe@Bloomberg.net

Last Updated: March 28, 2005 00:33 EST

Bruce

From: Rep. Bruce Weyhrauch [Representative_Bruce_Weyhrauch@legis.state.ak.us]
Sent: Thursday, June 23, 2005 8:57 AM
To: Bruce Weyhrauch
Subject: FW: The Economist, :(reading

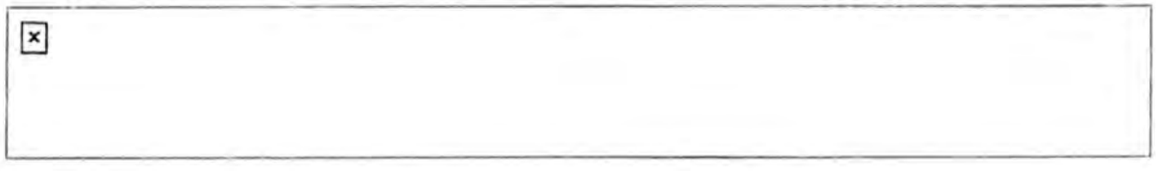
From: Brad Fluetsch [mailto:bjf@gci.net]
Sent: Tuesday, June 21, 2005 4:30 PM
To: Rep. Bruce Weyhrauch; Rep. Beth Kerttula; Sen. Kim Elton
Subject: The Economist, :(reading

Buttonwood

S&L redux

Jun 21st 2005
From The Economist Global Agenda

Who should be responsible for honouring the promises that companies make to their workers?



BUTTONWOOD is not exactly counting the grey hairs yet. But in the unlikely event that her children ever finish their hugely expensive education, it would be nice to think that she could hang up her keyboard one day and devote herself to Sudokus. The way company pension funds are going—and *The Economist*'s is better than most—that day looks increasingly remote.

It's not just the headline problem-kids—MG Rover, the British carmaker that went bust this year stranding 5,000 workers; America's United Airlines, which tossed its 120,000 workers at the Pension Benefit Guaranty Corporation (PBGC) in May and ran, in the biggest pension default in history; or General Motors, borrowing to pay the pensions of workers as it fights for its life. The issue is broader.

Pension plans depend on company contributions and investment returns for their funding. Actuaries' assessments of mortality rates give a guide to future liabilities. Bond yields provide the discount rate that broadly determines what current assets the plans must hold in order to meet those liabilities. The situation has been dire all round. Returns on investment have been lower than expected. Bond yields have been too, thus swelling the amount of current assets plans must hold.

Beneficiaries are living longer than anyone thought they would.

True, companies could have spent more of their recent record profits topping up their pension plans and less of them pleasing shareholders with dividend increases and share buybacks. But they have at least been paying more in. Employer contributions have shot up in Britain; last year, for example, firms contributed £25.6 billion ($47 billion), compared with £20.9 billion the previous year, and a steady level of around £7 billion in the 1990s (almost all of the money goes to defined-benefit schemes). The trouble is that liabilities have shot up faster.

In Britain, defined-benefit pension funds of FTSE 350 firms were around £70 billion short of where new international accounting standards say they should have been at the end of May, on figures from Watson Wyatt, a firm of actuaries. A broader definition of full funding puts the shortfall at £197 billion. Pension legislation enacted in 2003 and 2004 has broadly tightened funding, but these baked-in deficits are huge and so is the anxiety they generate. The only worry that is not yet on many lips is that taxpayers might have to underwrite the Pension Protection Fund if too many pension schemes go into default.

Not so in America, where people are speaking openly of a taxpayer bail-out to rival the rescue of America's savings-and-loan (S&L) sector in the late 1980s. The pensions insured with the PBGC showed a shortfall of almost $354 billion at the end of the last fiscal year, compared with $279 billion a year earlier. If the deficits of less underfunded plans are rolled in, the total shortfall is more than $450 billion. The PBGC had a $23.3 billion deficit last year in its main programme. Premiums do not keep pace with expected claims, still less reduce the accumulated shortfall. An independent think-tank, the Centre on Federal Financial Institutions (COFFI), said this week that the PBGC needs an infusion of $92 billion in today's dollars to meet its future obligations.

And the problem can only get worse. America's defined-benefit schemes tend to be more concentrated than Britain's in the unionised and industrial sectors that have been most buffeted by competition of one sort or another lately. Delta Airlines threatens to follow US Airways and United Airlines into bankruptcy and pension default. Ford, GM and DaimlerChrysler have among them hundreds of thousands of pensionable employees and retired workers. More generally, the number of those receiving benefits is increasing, while the number of active workers in defined-benefit schemes is falling. This adds to the pressure.

Companies and asset managers have tended to take a laid-back approach to pension underfunding, relying on the markets to right things as they often have before. What is worrying about the latest numbers is that we are seeing them towards the end of a period of strong economic growth and corporate profitability, neither of which is likely to continue. John Mauldin, an investment consultant, calculated in a recent column that total portfolio returns over the next ten years were likely to be around 5%, far less than the 8-9% projected by most funds. He reckoned that the total shortfall in America could be somewhere between $500 billion and $750 billion. And that is without counting companies' promises to provide health care to employees and retired workers. Nicholas Colas at Rochdale Research, an independent firm, calls these obligations a bigger problem than pensions because they are neither funded nor insured.

What is worrying about the latest numbers is that we are seeing them towards the end of a period of strong economic growth and corporate profitability, neither of which is likely to continue

There are a couple of weird circularities here. Most of the burden of filling these gaps will fall on the companies themselves, which will depress their profits. That, in turn, will depress share prices, which will make it harder to achieve adequate investment returns. And if asset managers turn en masse to bonds with long maturities to match their assets and liabilities more precisely, which is necessary especially for older plans, that will raise bond prices, depress bond yields and increase the present value of assets they must hold—again, widening the pensions gap. They could, of

course, look to other asset classes that pay higher or "absolute" returns (hedge funds of funds, private equity, property) and many are doing so. But "alternative" assets do not typically account for more than one-tenth of the total portfolio, in part because they are labour-intensive to manage.

This is all looking dark, if not necessarily as bad as the S&L meltdown, which cost taxpayers $128 billion. It is especially bleak because it is forcing societies to establish difficult priorities. These "legacy costs" are, in a sense, the debt that the new economy owes the old one. But no one wants to pay it.

Should workers just be forced to accept the bad hand that fate dealt them? That looks rash as well as unfair: in America, the workers who would be thus left to their own devices fall disproportionately in swing electoral states such as Michigan, Ohio and Florida. Should a company's current shareholders bear the brunt? If so, more firms than ever will close their defined-benefit schemes (in America, only about a fifth of all workers are covered by one now) and the investment risk inherent in saving for retirement will fall on the untrained individual. Or the taxpayer could foot the bill—but both America and Britain (indeed, most governments in most places) are printing money as it is. As COFFI's Douglas Elliott says, "All the choices are ugly."

Send comments on this article to Buttonwood (Please state whether you are happy for your comments to be published)

Read more Buttonwood columns at www.economist.com/buttonwood

Copyright © 2005 The Economist Newspaper and The Economist Group. All rights reserved.

PV=(I-C)(i)^2+-L*(i^2)^2+A*i
bjf

Ginny Austerman

From: Bruce Weyhrauch [whyrock@gci.net]
Sent: Monday, July 25, 2005 11:48 PM
To: Ginny Austerman
Subject: *****SPAM***** FW: New Jersey pension problems

file

From: Brad Fluetsch [mailto:bjf@gci.net]
Sent: Monday, July 25, 2005 5:41 AM
To: 'Bruce Weyhrauch'
Subject: New Jersey pension problems

N.J. taxpayers face a pension bill of $383 million

Saturday, July 23, 2005
BY DUNSTAN McNICHOL
Star-Ledger Staff

Pension costs for municipal workers, police and firefighters have more than doubled this year, leaving local taxpayers facing a bill of $383 million in budgets that will be drawn up early next year, state officials announced yesterday.

"Quite frankly, they took my breath away," Bill Dressel, executive director of the New Jersey State League of Municipalities, said of the new pension costs, which were announced late yesterday. "These are astronomical increases."

State Treasury officials said the new pension bills -- an increase of $208 million over the amount local taxpayers had to pay this year -- would have been far higher except for a policy of phasing in the retirement costs over five years.

"But for the phase-in, taxpayers would have felt a much more significant impact," said Treasury spokesman Tom Vincz. "We provided as much notice as possible for them (local officials) to make plans."

The new pension payments are due from towns next April. They will have to be included in municipal budgets next year, a fact Dressel said will likely lead to local property tax hikes.

"The magnitude of the increases and the fact we have gotten no state aid increases this year magnifies the problem," said Dressel. "I think this is going to be a shocker."

For local government officials, the pension bills are a relatively new entry on their balance sheets. Before this year, local governments had gone six years without having to pay anything toward their employees' retirement programs. Instead, state financing maneuvers and a soaring stock market had generated surpluses that offset the need for new contributions.

But that changed dramatically with the collapse of the stock market in 2002. State Treasurer John McCormac told lawmakers during budget hearings this spring that the state and local retirement systems are now underfunded by as much as $35 billion -- a deficit that must be made up by investment gains or contributions over the next three decades.

For local governments that means the cost of pensions is suddenly becoming a big-ticket budget item.

In Newark, for instance, the bill for pensions will jump from $9.6 million this year to $20.2 million. West Orange, the hometown of acting Gov. Richard Codey, will owe $1.9 million in pension payments next year -- $1 million more than the township paid this year.

Statewide, the bill for pension contributions that local taxpayers must fund has jumped from $175 million this year to $383 million for next year. And that is only the start of a trend.

Under the state's phase-in program, towns have been billed only 40 percent of the actual tab they owe for their non-uniformed public employees and 60 percent of what is due for the police and firefighters' system. In upcoming years the portion billed is scheduled to rise by 20 percent annually, and because of lower than projected investment gains, the total bill is also on track to keep growing.

"It's absolutely clear to me that I'm going to have to think of some way to soften the impact of these costs between now and April," Dressel said.

PV=(I-C)(i)^2+-L*(i^2)^2+A*i
bjf

Voice of the Times
A CONSERVATIVE VOICE FOR ALASKANS

WILLIAM J. TOBIN
Senior editor

PERS/TRS reform becomes reality

By RAYMOND MATIASHOWSKI



Shortly after Gov. Frank H. Murkowski took office in 2002, we learned that we had inherited a Public Employees' Retirement System and Teachers' Retirement System that had an unfunded pension liability of more than $4 billion. Today the underfunding stands at $5.7 billion.

We went to work and Gov. Murkowski is about to sign landmark legislation implementing much-needed PERS/TRS reform. The measure originated in the Alaska State Senate and passed during the special legislative session.

PERS and TRS reform fully protects the existing retirement benefits for all current and retired state employees. Nothing changes for Alaska's current public sector workers or teachers.

For employees hired after July 1, 2006, the reform measure replaces the existing defined benefit plan familiar to state workers with a new defined contribution plan similar to the 401(k) plans used by federal and many private sector employers.

The defined contribution plan provides comprehensive retirement benefits for future state employees and is a recruiting tool for the professionals we depend on for effective state government.

Gov. Murkowski will make history when he adds his signature to PERS and TRS reform. The measure recognizes flaws in a system that was increasingly unstable financially and losing the ability to meet the needs and expectations of employees and employers.

To deny that Alaska's pension plan was troubled and more than $5 billion-plus underfunded was to ignore reality. And make no mistake, the state has a constitutional obligation to make sure pension benefits earned under the existing system are paid.

First it was urgent that we stop the hemorrhaging of red ink. Now policymakers can move on to craft a solution that will address the unfunded liability. We will continue to work closely with the Legislature, including the House Special Committee on Ways and Means that is holding a series of meetings and hearings during the interim until the next session convenes on January 9.

Today, America is a nation of constant change and movement. Location and lifestyle changes are the norm rather than the exception. Research indicates that young workers entering the workforce recognize that the defined contribution is an attractive plan.

If a young family is thinking of moving north for work in Alaska, the new defined contribution offers more flexibility than the dated defined benefit program.

For a future state employee, the employer and employee will make contributions totaling 13 percent of his or her paycheck into the defined contribution plan. In addition, the employer and employee will set aside a combined 12.26 percent of the employee's wages into the supplemental benefits annuity plan.

Together, these two plans — comprising employer and employee contributions — will represent a total of 25.26 percent of an employee's payroll for future retirement benefits.

Like a 401(k) plan, the defined contribution is portable with many employers when jobs or careers change. Benefits are protected for employees and families and throughout careers.

PERS and TRS reform stabilizes the system and reduces financial volatility with a new Alaska Retirement Management Board. ARMB members take up their duties on Oct. 1 of this year.

The new board combines the functions of separate boards for PERS, TRS and the Alaska State Pension Investment Board that were responsible for $12 billion in pension investments. Under the former structure, one board dealt exclusively with the assets while the other two boards were responsible for the liabilities of the retirement systems.

This created an inherent disconnect. The new board resolves this problem by making one board responsible for both assets and liabilities.

A common question during the PERS and TRS reform debate was, "Can't we just wait and get another opinion?"

Until recently, General Motors may have thought it could "just wait." But now GM has said it must lay off 25,000 workers. Standard & Poor's had downgraded some GM debt to junk bond status, worker pensions were underfunded and health care costs were out of control.

Alaska will not "just wait." We will not let our state be vulnerable to billion-dollar liabilities that put taxpayers at risk of massive tax increases.

Raymond Matiashowski is commissioner of the Alaska Department of Administration.

The Anchorage Times

Editors: TOM BRENNAN, 264-8191; PAUL JENKINS, 264-8192; WILLIAM J. TOBIN, 264-8193.
Associate editor: IAN SINCLAIR, 264-8107 • P.O. Box 100040, Anchorage, AK 99510 • FAX: 907-264-8104

The Voice of the Times does not represent the views of the Anchorage Daily News. It is published

THE BOND BUYER online
www.bondbuyer.com

REGIONAL NEWS

E-mail this article

Vermont Probes Near-Universal Problem of Underfunded Pensions

Posted 07/26/05

By Helen Chang

RELATED STORIES

- Panelists Discuss Benefits and Pitfalls of Issuing Bonds for Pension Funds
- Panelists Cautious About Using POBs for Pension Liability Relief
- Hedging on Pensions
- Pension Woes Hard To Assess

A special commission of Vermont officials met for the first time this week to tackle a problem that, according to one study, afflicts 94% of all public pension programs: underfunded liabilities.

Vermont Treasurer Jeb Spaulding said the retirement systems his office manages — the state, municipal, and teachers pension systems that altogether have 24,027 active and 9,318 retired members — are ripe candidates for reform. Even as the costs of retirement plans and post-employment benefits soar, state and local governments are pressed to match pension demands with tax dollars and investments that failed to perform to expectations. It's a problem with no clear or easy solutions.

"Without the study, it will be much harder to find the political will necessary to make changes," Spaulding said. "Our funding status isn't anywhere near what people think it is, so I'm anticipating this will be an interesting exercise."

Vermont will be reviewing its pension benefits and how they compare to other public retirement systems, and whether they are consistent with the state's demographic trends. Spaulding said he would also consider new options for paying for pensions, including requiring local

OTHER T

- MSA B as Gro for Big Fines
- Wisco Veto t Bienni
- Morga Ex-Mo Farrell
- Cox W Hearin SEC Ne
- N.Y. Ja Agenc Bond f
- N.Y. D Decide for Bro

government contributions, selling pension obligation bonds, or re-amortizing the pension systems' unfunded liability.

Vermont may discover, as other states have, that it owes retirees more than expected.

Rhode Island, for example, earlier this month decided to reduce pensions for future and existing public employees. Lawmakers there reduced some state employee and teachers retirement benefits after a pension review committee's report "opened their eyes to the huge costs they'd be hit with if nothing changed," one state official said. Rhode Island's unfunded pension liability for state workers and teachers is estimated at $3.5 billion — more than half its $6.35 billion annual budget.

Officials say the reforms, which only apply to state employees and teachers with less than 10 years of service, will immediately save the Rhode Island and its local governments $44 million this year and $270 million over the next five years. Rhode Island's local governments contribute 60% towards the teachers pension system.

For the first time since 1984, Rhode Island lawmakers established a minimum retirement age. Cost of living increases, previously set at 3%, are now pegged to inflation with a 3% ceiling. Benefit levels were also reduced. Current retirees with more than 35 years of service now receive 80% of their base salary. New retirees can now expect 75% after 38 years of service.

Not surprisingly, the move has elicited criticism.

"It's a terrible outcome and well beyond what we think is fair," said Bob Walsh, executive director of the National Education Association of Rhode Island. "A teacher coming in under the new system, and paying 9.5% salary contribution over 38 years to maximize benefits, will have paid the entire pension benefit themselves [by the time they retire]."

Standard & Poor's analyst Parry Young estimates Rhode Island is only the second state to reduce its pension benefits, after Oregon. Unfunded pension liabilities are also squeezing states and localities' budgets elsewhere in the Northeast, rating agencies said. Connecticut, which faced a $1.1 billion budget gap this year, has a $12

billion unfunded liability from its state employees and teachers retirements systems, according to Fitch Ratings. Massachusetts' unfunded liability is similarly sized, according to Standard & Poor's.

In a nationwide survey of 109 state retirement systems, investment management and consulting firm Wilshire Associates Inc. found that 94% are underfunded, though funding ratios have improved alongside recent gains in the stock market.

Despite the apparently broad reach of the problem, few states so far have undertaken structural pension reforms. Reform is often a politically sticky affair as public officials must balance their fiduciary responsibilities with retirees' demands, which are often backed by politically strong unions. Oregon, which also sold pension obligation bonds to reduce its liabilities, emerged from a two-year legal battle with public employee unions last month when its state Supreme Court upheld many of the structural changes lawmakers made to the pension system in 2003, according to pension spokesman David Crosley.

Rhode Island's reforms follow a 77-page report and a year-long study by a pension review committee created by Republican Gov. Donald Carcieri in 2003. All 12 committee members, six representing labor interests and the others the administration and local management, agreed that reform was necessary, though only half approved the report's recommendations, said committee chairman Jerome Williams, who also serves as the executive director of the state's Department of Administration.

While Rhode Island requires employees to pay some of the highest contributions to their pensions in the country, the benefits paid out were generous when compared to other systems. Rhode Island's pensions offered a 3% annual cost of living increases, adjustments found in only 16% of other plans surveyed. The retirement system lacked a minimum retirement age, which encouraged workers to retire earlier. The average retirement age for teachers in 1993, for example, was 60. Now it's 56.

Demographic trends were also found to increase pressure on pension systems as retirees are proportionally growing faster than active workers. In Rhode Island's teachers system, which has 14,710 active and 7,310 retired members, retirees are increasing at 5.7% compared to

active members' 2.9%. In the state workers system, with 13,795 active and 9,426 retired members, active members are growing at 1%, compared to 1.5% for retirees.

Pension committee members had briefly considered issuing POBs, but were daunted by the size of a potentially $500 million issue. Last year, the state roughly had $720 million of outstanding GO debt.

"It just wasn't feasible," Williams said. "One of the things we pride ourselves in is our credit rating, and we didn't want to impact our ability to issue debt in the future."

Additionally, POBs haven't always worked out as intended. The bonds reduce management's flexibility, in that it turns the unfunded liability "soft debt" into "hard debt." POBs are also a gamble because the investment proceeds from the bonds may not yield more than the bonds' original interest rate. Pension system officials considering such a tack should consider Worcester, Mass.

Worcester has incurred a significant additional liability on its roughly $220 million of POBs sold in 1998, due to lower than expected investment returns. The POBs now represent 34.5% of the city's outstanding debt, according to Moody's.

Worcester's retirement system became fully funded after its bond sale. However, the retirement system's unfunded pension liability has now grown to $160 million, thanks to poor stock market investment returns and expanded retiree benefits, according to the Worcester Regional Research Bureau.

click here for information about Article Reprint permissions.

E-mail this article

Copyright © 1997-2005 The Bond Buyer. All Rights Reserved.

YOU ARE ENTITLED TO DISPLAY AND SEARCH THE CONTENT OF THIS SERVICE AT THE TERMINAL ACCESSING OUR SITE, AND TO DOWNLOAD ARTICLES, SOLELY FOR YOUR OWN PERSONAL USAGE. NO PART OF THIS SERVICE OR CONTENT CONTAINED HEREIN MAY BE OTHERWISE RETRANSMITTED, REDISTRIBUTED, COPIED, STORED, DOWNLOADED, ABSTRACTED, DISSEMINATED, CIRCULATED OR INCLUDED AS PART OF ANY OTHER PRODUCT OR SERVICE.

PLANSPONSOR.com Don't go it alone Magazine

Their Own Worst Enemy

Why are so many public plans in trouble?

Their Own Worst Enemy

Why are so many public plans in trouble?

"I do not know if we invented the process of skipping out on pension obligations, but we sure perfected it," says Ralph Martire about the state of Illinois and its politicians. "We are the masters of the politically expedient."

State law requires balancing the budget each year, and Illinois legislators have a perennial problem because the state has not broadened its revenue base enough, says Martire, executive director of The Center for Tax and Budget Accountability, a bipartisan think tank based in Chicago. "The alternatives are that they can raise taxes or raid the pension funds again. So, they dip into the pension funds to avoid painful spending cuts," he says. "This year, they did not fund the pension contribution at all. It saved them $2.4 billion."

The consequence, according to Martire: "We have the biggest pension underfunding of any state in the nation. It is $38 billion and growing. We have a bigger unfunded obligation than New York, Texas, Florida, or California. It is outrageous. This is not a partisan problem: Republicans and Democrats are equally culpable of resorting to feckless measures to balance the books, and their failure is haunting us now."

Public pension funds had an aggregate funding ratio of 88.2% in fiscal 2004, says Keith Brainard, Austin, Texas-based research director for the National Association of State Retirement Administrators. That number, which includes primarily state funds but also some local funds, compares with 101% in fiscal 2001. "[The current funding ratio] is going to be right about the low point, assuming investment returns stay in their normal range," he speculates.

Moreover, the official numbers may underestimate the depth of the problem, according to a study by Barclays Global Investors. If public plans used the same accounting rules as private plans, their underfunding would total about $560 billion rather than the reported $278 billion, the study found. The reason: FAS 87 stipulates that private plans use different rates for the assumed investment return and the discount rate for calculating liabilities, while Government Accounting Standards Board regulations mandate that public plans utilize the same interest rate for both, says Matthew Scanlan, a San Francisco-based managing director at BGI. As he says, "It has a huge effect."

There has been lots of talk about how poor stock market returns and low interest rates led to problems for pension plans. However, there has been less light shed on another major contributor to the dilemmas faced by public plans: politicians.

"The funding mechanism is controlled by politics," says Fred Nesbitt, executive director and legislative counsel at the National Conference on Public Employee Retirement Systems in Washington. "If politicians increase the benefits but do not increase the funding, that is going to catch up with them. If they are enjoying pension 'holidays,' they should not be surprised if they have to contribute more later. In California, where Governor Terminator is saying, 'Oh, it is costing us too much money,' he forgets to mention the five years when employers and taxpayers did not have to make a contribution."

Still, most public plans are in OK shape, Nesbitt believes. Where big problems exist, he says, "It is not because the trustees are irresponsible. It is not because defined benefit plans do not work. It is because people manipulate the plans for political purposes—- and it is coming back to haunt us."

top

Low Contributions + High Benefits = Trouble

Low Contributions + High Benefits = Trouble

Public plans' current troubles often boil down to too-low contributions or too-high benefit increases—or both. Politicians have a lot of influence on each.

The stock market's boom got politicos addicted to scant contributions. "[They] quickly got accustomed to low contributions, or no contributions," Brainard says. In states like New York and California, he adds, employer contribution rates drifted down to "near zero and, in some cases, zero."

ERISA governs contribution levels for private plans, but those rules do not apply in the public sector, says Steven Foresti, managing director at Wilshire Associates Inc. in Santa Monica, California. "For public plans, it depends state by state, municipality by municipality," he says. "The guidelines in terms of contributions are vastly different."

The market's boom led to another ill-fated move for many public plans. "Suddenly, funding the future commitments seemed a lot less expensive. So, there was pressure to increase benefits," Foresti says. After all, public-employee unions form a powerful voting block.

"Benefits were increased at a time when assets were at a high," Foresti says. "All it takes is a downturn in the markets to reveal the true costs of funding these benefits." Politicians sometimes increased pension benefits with a philosophy of "We will pay for that later," Scanlan says. "Pension plans have overpromised benefits—and a lot of those pension promises are coming due."

top

Four Places Where It Happened

Four Places Where It Happened

A bunch of state and local plans have found themselves needing to put up big contribution bucks. Brainard puts it simply: "The bottom fell out of the market. So, contributions have leaped." Here are four of those stories:

New Jersey. The $70 billion New Jersey Public Employees' Retirement System (PERS) faces serious trouble. "[The plan's underfunding] is about $25 billion," New Jersey State Treasurer John McCormac says. "Depending on the assumptions you use, it could be as high as $30 billion."

The trouble largely stems from the 1997 decision by then-governor Christie Whitman to float $2.8 billion in 30-year bonds to pay off the state's underfunded pension. The idea: that the state could use the proceeds to earn more in the then-hot stock market than the 7.64% it had to pay out in interest on the bonds.

"The plan was that it would wipe out pension contributions for the foreseeable future," McCormac says. "It is essentially a 30-year bet that you can earn more on the pension investments than the yield on the bonds."

That worked well for a few years, until the stock market tanked. Now, the state not only owes

the principle and interest on the bonds, but also faces big funding payments into the pension system.

"We still owe $10 billion in principle and interest on those bonds," McCormac says. The actuary for the state's six pension- systems estimates that the state will have to contribute $1 billion to the plans in 2007, he says.

Why would anyone make such a risky move? Whitman was running for reelection at the time, and wanted to cut taxes rather than use the money to fund the pension. Asked if he thinks that politics motivated the decision, McCormac says, "You draw your own conclusions." Nesbitt puts it more bluntly, saying, "The pension system there has been robbed."

Now, New Jersey has to try to dig out. The solutions include diversifying its investments more, McCormac says. PERS has not been meeting its annual assumed return, he says, which was 8.75% until it was lowered to 8.25% earlier this year.

The retirement system invests two-thirds of its money in stocks and one-third in bonds, he says, while "every other major plan in the country has alternative investments."

New Jersey has taken criticism in the past for some archaic policies, including not hiring any outside managers and only trading on Tuesdays. The Tuesday mandate is history now. The investment diversification project started in June, and the Investment Council approved the first three investments in private equity. These investments cannot be managed in-house by the Division of Investment staff, a Treasury spokesperson says.

In May, acting New Jersey Governor Richard Codey named an eight-member Benefits Review Task Force to recommend ways to deal with the escalating cost of the state's benefit programs. McCormac will not comment on the possible retirement plan changes, but sources say that they could include converting new employees to a defined contribution plan going forward.

San Diego. The San Diego City Employees' Retirement System- faces a $1.4 billion deficit, and Mayor Dick Murphy announced his resignation earlier this year as the criticism mounted. Tensions are running high at the City by the Sea, where the Securities and Exchange Commission has issued subpoenas, and the District Attorney has filed criminal charges against seven pension board members for their role in boosting pension benefits (including their own). A handful of city retirees has even filed suit against the city's pension actuary for his alleged role in obfuscating the impact of changes in the pension program.

"The problem is not public employees," says Steven Erie, a professor of political science at the University of California, San Diego, and a long-time watcher of the city's political scene. "The real problem in San Diego is cheap voters and cowardly politicians."

The trouble started a while back, Erie says, when the city failed to diversify its revenue sources enough after state voters, in 1978, approved the Proposition 13 initiative limiting property tax rates. "The last 20 years, we should have had an honest discussion about raising taxes and revenues," he says.

So, city politicians siphoned off pension surpluses during the 1990s to the city's general revenue fund, Erie says, on the rationale that the booming stock market meant that the fund did not require more than the minimum contribution. "San Diego put all its eggs in one basket: the pension," he says. "This was the goose that laid the golden egg."

During that same time, Erie says, local politicos also increased public workers' retirement benefits. "Because of the political culture in San Diego, we do not give employees much in the way of salary increases," Erie says. In May, Murphy announced a three-year labor deal with the San Diego Municipal Employees Association that calls for a salary freeze during the first two years and a 4% salary boost during the third year. "We backload it with pension increases, so that it does not show up in the budget today. It is a classic strategy"—a

strategy that increased the pension plan's liabilities.

Given those political decisions, Erie says, it is no surprise that the finances of the city and its pension fund went south when the stock market did. "The chickens," he says, "have come home to roost."

Houston. Like San Diego, Houston made a dubious boom-time decision to raise city employees' retirement benefits. The Houston Municipal Employees Pension System went from 91% funded in 2000 to 60% funded in 2002. "It was a function of benefit enhancements," says Joseph Esuchanko, an actuarial consultant hired by the city administration to study the problem.

In 1998, the city had set up a deferred retirement option plan (DROP) within its defined benefit plan that let city employees take retirement when they were eligible but stay on the job. Under this option, an employee's monthly retirement, earned as of the effective date of DROP participation, is credited to his DROP account. While the employee continues to work, he or she earns no additional retirement credits. However, his DROP account is credited with the contributions he would otherwise make to the pension plan, interest at a minimum rate of 8.5% (compounded daily), and an annual 4% cost of living adjustment. The pension the DROP participant receives, over and above his DROP account when he retires, is sometimes greater than what he would have received if he had not participated in the DROP.

Between 1993 and 2001, the city thrice raised the accrual percentage for calculating benefits. During that time, for instance, the percentage for those with 25 years of service jumped from 52.5% to 88.75%. This was a 69% increase in pension, compared to a 23% increase in the Consumer Price Index during that time.

The plan's actuary initially made assumptions about the DROP that proved too upbeat, says Esuchanko, president of Troy, Michigan-based Actuarial Service Co. In 2001, the plan's actuary continued to assume limited participation in the DROP, based on past experience, even though the incentive for participating in the DROP had increased substantially. "If the actuary uses extremely optimistic assumptions, it appears that the cost will be significantly less than it actually will be," he says.

Not surprisingly, then, the new setup could lead to some big benefits. Esuchanko's study included what he calls a "worst-case scenario." Say a 46-year-old Houston city employee hired at age 22 and making $40,000 annually had taken the DROP option. If that person continued working for the city until age 65, the DROP account would have grown at 11.1% interest to a staggering $2.75 million. "This person would have a replacement ratio at retirement of 455%," he adds.

In 2000, the study says, the city's contribution to its pension plan totaled 9.5% of member payroll. Two years later, the number had grown to 31.8%. By that time, the unfunded liability had skyrocketed from $133 million in 2000 to $995 million, Esuchanko says. Last year, the city's voters approved a measure that excused the city from a state law preventing reductions in the pensions of city employees. Subsequently, changes were made that returned the pension formula to pre-2001 rates and removed many of the DROP incentives. Those changes substantially reduced the financial burden on taxpayers, he says.

Alaska. In the case of the state of Alaska, legislators rather than voters decided to make a change prompted by a pension cash crunch. This May, they voted to put all new state and local govern-ment hires as of July 2006 into a defined contribution plan. The reason: a $5.7 billion total funding shortfall in the Alaska Public Employees' Retirement System (PERS) and the Teachers' Retire--ment System (TRS).

The financial crunch stems from two factors, says Esuchanko, who was hired by a state legislative committee to study the situation. First, the state's pension funds had poor investment returns- as the stock market turned unpredictable. Second, Alaska takes the

unusual step of pre-funding its post-employment health care through the pension plan; that policy cannot be changed because a state law prohibits taking away any future benefits promised to state workers, he says. "With the rising cost of health care, the liability has grown astronomically," he adds.

Not everybody thinks the defined benefit plans were hopeless. The Alaska legislature's switch to a defined contribution was "purely political," Nesbitt believes. "The pension funds had a $5 billion shortfall, and they used that as a way of destroying the pension funds. They will live to regret it, because they will have a problem with hiring and retaining state employees."

Esuchanko does not paint such a dire picture, but he agrees that the move does not make the state's problem disappear. "Certainly not in the short term, because they have got all these people in the defined benefit plan," he says, "and, five years from now, the vast majority of employees will still be in the defined plan."

top

SIDEBAR: Out of Control?

GASB shift could mean trouble for government health-care programs

The sound of distant thunder heard today at many city and state government offices is not coming from a summer storm. Instead, it is coming from the Norwalk, Connecticut based Government Accounting Standards Board as the deadline nears for the enactment of Statements 43 and 45.

Back in February 2003, GASB officials decided it was time for state and local governments to join their corporate brethren and report the accrued liabilities for what are referred to as "other post employment benefits" or OPEB. As most of these benefits are ever increasing retiree health-care costs, the added burden of reporting them as they are accrued rather than the long-time, "pay-as-you-go" method could deliver a blow to municipalities. To quote one city official, "It would take our credit rating and flush it down the toilet."

How many municipalities will the GASB changes affect? According to the International City/County Management Association Retirement Corporation (ICMA-RC), 60% of city and county governments provide health-care benefits to retirees. Of those, about one-third pay 100% of benefits; one-third share the cost with retirees, and another third are entirely retiree-funded. Adding to the burden on employers—and retirees—is the continuing escalation in the cost of these benefits. ICMA-RC found that, in 2003, the average cost to insure an individual was 62.5% higher than it had been in 1998. Local governments are going to have to be creative in planning to account for the full cost of accrued retiree health benefits or risk jeopardizing their bond credit rating.

Officials in Orem, Utah, are well along in planning for the change. Back in 1982, city employees were given a retiree health-benefit plan in which the city paid 75% of the premium for eligible retired employees and their dependents, with single or family coverage. Orem, with a population of 90,000, currently has 420 benefit-eligible employees and 51 retirees receiving retiree health-care coverage. However, "If everyone retired who could, the group of 51 would become 125 retired and their dependents," notes Assistant Deputy City Manager Richard Manning.

"The change to GASB caught a lot of people by surprise," he believes, and city officials quickly turned to the Salt Lake City office of Milliman (USA) Associates for an actuarial study of the retiree health plan. The study revealed that, as of January 1, 2004, the city needed to put $14.8 million in a trust account and add $800,000 more each year to get the plan fully funded—not likely with an annual city budget of $60 million.

"For the past eight months, we have been devising an exit strategy for our defined benefit

health-care plan," Manning continues. In 10 separate meetings—with city council members, employees, and retirees—Orem officials, working with their health-plan provider, ICMA-RC, worked on a transition plan. Although the plan has not yet been officially adopted—the city has until July 1, 2007, to begin complying with the new GASB rules, after all —the basic outline has been reached. For the next 15 years, through 2020, the city will move away from the current 75% premium payment defined benefit while allocating a block of money to pay for that premium each year to eventually fund the current commitment. Next year $280,000 will be set aside. The 15-year phaseout will feature an annual allocation for funding to be distributed to qualified retired employees to assist them in paying their health-care premiums.

Just as the trend in pensions has been a migration from defined benefit to defined contribution, Orem is setting up its own version of a consumer-directed health-care (CDHC) plan called the Retiree Health Savings Plan. Beginning in 2006, current employees will contribute to the plan with a salary deferral that the city capped at 5% of pay. Participants select investment options such as mutual funds. Contributions, earnings, and distributions are tax-exempt for both the participant and the city. Another new benefit is an unused sick leave buy-back. Employees can have slightly more than 1% of annual salary donated to the plan for them each year that they do not use their sick leave. If they do use some of it, then 25% of the current year's unused sick leave can be donated to the health savings account.

The advent of accrual accounting for retiree health benefits does not bode well for defined benefit health plans at government employers. Back in 1990, the Financial Accounting Standards Board (FASB), which oversees the corporate world, issued FAS No. 106 requiring private employers to account for OPEB. Notes Kathy Harm, director of retiree health at ICMA-RC, "[That reporting requirement] is, in part, responsible for the significant drop in the availability of employer provided retiree health care in the private sector." In 1988, 66% of firms with more than 200 workers provided some health-care benefits to retirees. By 2002, the number had dropped to 34%, and that does not take into account reductions in coverage among that 34%.

GASB 45 will go into effect at various time intervals, depending on fiscal year and size of the employer, beginning after December 15, 2006. Many employers will not be affected until July 1, 2007. "While the actuarial liabilities associated with governmental retiree health benefits are significant, it's important to understand that the employer's financial statement liability (i.e., the 'net OPEB obligation') will accumulate gradually over time as the difference between annually required OPEB contributions and contributions actually made materializes," explains Brian Murphy, senior actuary and president of Gabriel, Roeder, Smith & Company. "Governmental employers have time to consider how they will deal with the issue," he believes.

Whether or not there will be an effect on the employer's credit rating remains to be seen, Murphy continues, but initially, at least, implementation of GASB's OPEB rules will affect many governments in a similar manner. Benefit changes are likely and, in some cases, already are under way. It is difficult to determine how this will evolve, but it will likely involve additional costs borne by the participants and some movement toward defined contribution-type plans, like health savings accounts, for retiree health care. The extent to which these types of plans will become substitutes for traditional health-care coverage is unclear, Murphy concludes.

Employers that historically avoided a defined benefit health plan are in better shape to handle the GASB ruling. One such sponsor is Steve Purvis, director of special projects and internal audit for the city of Boise, Idaho. "We decided we should stay away from providing defined benefit-type health coverage for our employees, other than the Public Employee Retirement System of Idaho," Purvis explains. "We made the decision early on [in the early 1990s]. Looking at the numbers had to scare a finance guy to death," he gibes.

While the fire and police unions fought a hard battle for a defined benefit health plan, Purvis researched alternatives. He wanted to accomplish three things: get employees to save

money; make the money "do more" by allowing employees to select how they want to use the money in their accounts; and make participants more efficient users of the money. He also was looking for a more flexible plan than a defined benefit would allow. It turned out that Nationwide Financial's Post-Employment Health Plan (PEHP) fit their requirements.

Boise is a city with a population of close to 200,000, and has a full-time work force of approximately 1,500 employees, with 1,419 participating in the PEHP and 106 who have either retired or separated from service, and are receiving disbursements from the program.

The purchasing power of the participants was increased due to the fact that the funds going into the PEHP, accumulating, and coming out of the plan are tax exempt as long as they are used for qualified IRS medical expenses. One of the advantages of the PEHP design that is not talked about very much, Purvis feels, is the flexibility that it provides to participants as they use the funds. The participant gets to decide when the funds are used, how much are used, and on which IRS-qualified medical expenses they will be used.

As with other HRAs, the PEHP has been tailored to meet the city's needs. "We tried to design formulas that would allow more people to reach the minimum funding status of $44,500," says Purvis. The standard is an attempt to provide sufficient funds to pay 15 years of single person premiums to cover the gap between normal police and fire retirement at around age 52 to 54 and Medicare integration.- To meet the funding objective, several existing benefit programs were restructured. For example, a part—one-third—of the employer- 4.5% deferred compensation 457 plan match was redirected to the PEHP. The sick leave conversion benefit plan also was restructured and the funds put into the PEHP. The objective was to find various ways to provide funding for post-retirement medical costs. As medical costs continue to rise, the funding formulas need to be reviewed and adjusted.

An added benefit of restructuring the sick leave conversion plan was that, by automatically "sweeping" money out of the sick leave account and monetizing accumulated sick leave hours over a stated level annually rather than at retirement, employees felt an immediacy to the benefit, and sick leave utilization was reduced.

When it comes to complying- with GASB 43 and 45, Purvis notes that, while the police and fire retirees pay 100% of the active employee premium upon retirement, there will be some effect because the police and fire employees stay in the active employee medical plan from retirement until their Medicare integration dates, or around 10 to 12 years, a cost that is subsidized by the city and the active employees due to higher claims costs for retirees. Still, the effects will be mild compared to municipalities with defined benefit retiree health plans, notes Purvis.

top

Judy Ward
editors@plansponsor.com

Copyright © 1989-2005 Asset International, Inc. All rights reserved. No reproduction without prior authorization.

PERS and TRS Funding

Response to Questions

Alaska House of Representatives
Special Committee on
Ways and Means

Presented by

Department of Administration
Division of Retirement and Benefits

September 8, 2005

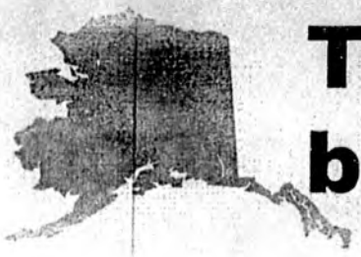


Questions posed from June 15, 2005, letter received from Represenative Weyhrauch. With respect to PERS and TRS, how are Tier I, II, and Tier III contributing to the deficit?



PERS 6/30/04 Accrued Liability by Tier (000's)

		Accrued Liability[1]	Percentage
Tier I	$	9,000,000	79.0%
Tier II	$	2,000,000	17.5%
Tier III	$	400,000	3.5%
Total	$	11,400,000	100.0%



TRS 6/30/04 Accrued Liability by Tier (000's)

		Accrued Liability[2]	Percentage
Tier I	$	5,550,000	90%
Tier II	$	600,000	10%
Total	$	6,150,000	100%

State of Alaska
DEPARTMENT OF ADMINISTRATION
DIVISION OF RETIREMENT AND BENEFITS

FRANK H. MURKOWSKI, GOVERNOR

PO BOX 110203
Juneau, AK 99811-0203
TDD: (907) 465-2805
FAX: (907) 465-3086
PHONE: (907) 465-4460
TOLL-FREE: 1-800-821-2251

September 7, 2005

The Honorable Bruce Weyhrauch
Chair Special Committee on Ways and Means
House of Representatives
State Capitol, Room 421
Juneau, AK 99801

Re: Response to Questions for September 8, 2005, Meeting

Dear Representative Weyhrauch:

This letter is written in response to the questions received from you on September 6, 2005. I have re-stated your questions below in italics with my responses immediately following.

1. *What is the present amount of the unfunded liability for PERS and TERS?*

   The draft valuation as of June 30, 2004, indicates the unfunded accrued liability for PERS is $3.4 billion and $2.3 billion for TRS. The total unfunded liability for both retirement systems is currently estimated at $5.7 billion. The next actuarial valuations for the systems using data as of June 30, 2005, will be available in April 2006.

2. *When we say unfunded liability what does that mean and is that* different *from using the words "deficit," "indebtedness," or "debt?"*

   The "unfunded liability" is defined as the excess of the accrued liability over the assets of the plan at the valuation date. Accrued liability is calculated at the valuation date and is the present value of benefits credited with respect to service earned to that date. "Deficit" is the amount by which a sum of money falls short of the required amount and "debt" is defined as an amount that is owed. It is not uncommon to have parties refer to unfunded liability, deficit, and the debt owed to the system. However, it is not common to hear the term "indebtedness" used when referring to the unfunded liability of the retirement systems.

   a. *How is it calculated?*

      Each year an actuarial valuation report is produced for the PERS and TRS retirement systems in order to obtain an up-to-date figure of the total liability for the entire system. An actuarial valuation produces an estimate of total liabilities, at a given point in time; however, it does not change the ultimate cost of the system. Actuarial valuations use assumptions to determine what the total cost

will be over the life of the system. These assumptions reflect the major variables that will affect total system costs, and the cost of any one individual. The actuarial valuation report determines the expected future obligation by measuring the plan liabilities and plan assets. The retirement plans funding ratio is determined by comparing the liabilities of the plan with the assets of the plan. A primary objective of the actuarial valuation report is to determine the employer contribution rate in order to fund and pay for future benefits.

b. *Is it likely that the events on which the calculation is based will occur?*

Every state in the country with an underfunded pension system has realized that assumptions used in the actuarial valuations and actual experience differ. Our goal is to select a qualified and professional actuary that will make estimates based on the best information available at the time.

3. *What does that liability mean in general and in particular for:*

a. *State finances*—Enclosed is information showing the projected costs through FY09 and the valuations show total employer contributions amounts through 2030.

b. *Credit rating*—This question would be more appropriately answered by the Department of Revenue.

c. *Additional appropriation*—In accordance with SB 141 the Alaska Retirement Management Board may end up recommending as part of its analysis of the retirement systems that additional appropriations are warranted to shore up the retirement systems.

d. *Retirees*—There will be no impact on retirees.

e. *Current employees here, especially with regard to take-home pay vs. total compensation, will pensions and health care costs for current employees or retirees be negatively affected by the liability.*—There is no direct impact on current employees; however, rising employer contribution rates will have an impact on future budgets. Response to impact for retirees is noted above.

f. *Payment of benefits (medical and pension)*—Retirees will continue to receive benefit payments for medical and pension.

4. *When did the unfunded liability begin and over what period of time has there been a liability?*

While the magnitude of the underfunded status was not known until April 2003 and after the start of this administration, many events over the last 10 years led to our current condition. It is difficult to pinpoint at what exact point the unfunded liability began, but our experience and audit of our actuaries have determined that (1) employer rates were reduced in the 1990s when investment returns were high, (2) medical assumptions starting in the late 1990s were too low, (3) investment returns in 2000, 2001, and 2002 did not meet the annual investment targets, and (4) the asset valuation method was changed as a result of the audit.

5. *When was the current magnitude of the present unfunded liability projected?*

See above—a copy of the 2002 actuarial valuation was finalized in April 2003, in accordance with the normal schedule for valuations.

6. *What is the division's position on the causes of the unfunded liability?*

Three primary factors contributed to the unfunded status: (1) rising health care costs; (2) loss of investment income; and (3) change in assumptions to reflect changing conditions.

Have actuaries done sensitivity analysis on various assumptions like rate of return on assets and rates of increase in medical costs?

The actuarial valuations do provide a sensitivity analysis regarding the effect on the retirement systems given specific key assumptions that involve the investment assumption, for example, the effect of investment returns of 7.5%, 8.25%, or 9.% for all future years (see enclosure). Additionally, the enclosed information shows what happens to the employer contribution rate if liabilities increase by 5% and as assets decrease by 5% (see enclosure).

7. *Should the legislature make an appropriation next year to reduce the liability?*

SB 141 prescribes that the Alaska Retirement Management Board will take up this question, "The Alaska Retirement Board shall report to the legislature . . .short-term and long-term recommendations for addressing the unfunded liability of the retirement plans."

8. *When does the legislature have to fund the liability or when will the legislature (and state) face a cash flow problem?*

The 5% annual contribution increase, in and of itself, creates a cash-flow problem for many PERS and TRS employers. As set out in the actuarial valuations for PERS and TRS, the actuary has recommended that the employer contribution rates go up to 28.19% for PERS and 41.78% for TRS as of the June 30, 2004, draft valuations. This increase results in TRS employer contributions increasing from $151 million in FY06 to $282 million in FY09, without any changes in services.

SB 141 superseded

It is expected that the employer contribution rates will continue to rise until they reach the calculated rate and remain at these levels for approximately twenty-five years, which is the amortized period to pay off the unfunded liability. Note: For every year that the employers are not contributing at the actuarially calculated rate it has the effect of increasing the unfunded liabilities of the retirement systems.

9. *Should the legislature worry about the liability or will it fix itself?*

According to Mark Johnson, Actuary with Milliam USA, in response to the question, "Can the CALTRS pension system invest its way out of its unfunded status?" Mr. Johnson concluded that the answer was "no." He said there was one chance in ten that CALTRS would be able to invest its way out of its underfunded status given the projections concerning future market conditions.

Basically there are three levers that could act to improve the systems underfunded status: (1) systems could experience higher investment returns than projected; (2) reduce benefits costs; or (3) receive a cash infusion in order to reduce or eliminate the unfunded liablity. SB 141 acts to address the future growth in the unfunded liability and also by establishing the Alaska Retirement Management Board it acts to address the unfunded liability for the systems.

10. *What approaches do you recommend to address the liability?*

As noted above, the division will await the report of the Alaska Retirement Management Board and its recommendations due to the legislature this session.

Please let me know if you have any questions about this correspondence.

Sincerely,

Melanie Millhorn
Director

MM/ck
Enclosures
cc: Members of Special Committee on Ways and Means

Ray Matiashowski, Commissioner
Department of Administration

Kevin Brooks, Deputy Commissioner
Department of Administration

Michael Tibbles, Deputy Commissioner
Department of Administration



Questions posed from June 15, 2005, letter received from Represenative Weyhrauch. With respect to PERS and TRS, what part of the unfunded liability is represented by health or retirement benefits?

PUBLIC EMPLOYEES' / TEACHERS' RETIREMENT SYSTEM
INFORMATION BRIEFING

SUBJECT: PERS / TRS Tier Classification Medical Benefits
DATE: JANUARY 10, 2005
NOTE: AS OF DECEMBER 2004 THERE ARE 27,095 PERS/TRS MEMBERS RECEIVING A RETIREMENT AND MEDICAL BENEFIT. IN ADDITION, THERE ARE 24,947 COVERED DEPENDENTS FOR A TOTAL OF 52,042 MEMBERS AND DEPENDENTS WITH MEDICAL COVERAGE.

PERS	Tier 1	Tier 2	Tier 3	Total
Active	7,916	9,086	16,878	33,880
Deferred Vested	2,864	2,785	393	6,042
Deferred	1,871	3,079	7,188	12,138
Retired	17,352	2,041	101	19,494
Total	30,003	16,991	24,560	71,554
Medical Benefits	System paid medical benefits for all benefit recipients and their eligible dependents. Eligible after vesting and normal retirement age of **55** or early retirement at age **50.**	System paid medical benefits for Police / Firefighters after 25 years or "all others" at 30 years of service. Eligible after vesting and age 60. Under 60 must pay premium. Disabilitants, regardless of age receive medical coverage.	System paid medical benefits for Police and Firefighters after 25 years or "all others" at 30 years of service. Eligible at age 60 after vesting; 10 years of credited service to qualify. Under age 60 must pay premium. Disabilitants, regardless of age receive medical coverage.	

TRS	Tier 1	Tier 2	Total
Active	3,204	7,037	10,241
Deferred Vested	404	259	663
Deferred	601	1,947	2,548
Retired	8,462	184	8,646
Total	12,671	9,427	22,098
Medical Benefits	System paid Medical benefits for all benefit recipients and their eligible dependents. Eligible after vesting and normal retirement age of **55** or early retirement at age **50.**	System paid medical benefits for teachers after 25 years of service. Eligible after vesting and age 60. Under 60 must pay premium. Disabilitants, regardless of age receive medical coverage.	

(Above member counts for both systems are as of October 11, 2004)
Note: Medical benefits account for a significant portion of the Systems liabilities.
PERS: 37% of accrued liability and 31% of accrued liability for TRS.



Liabilities Due to Pension and Medical (000's)

Accrued Liability

	PERS		TRS	
Non-medial	$7,189,244	63%	$4,216,480	69%
Medical	4,254,672	37%	1,907,120	31%
Total	$11,443,916		$6,123,600	

Alaska Public Employees' Retirement System - Teachers' Retirement System
Composite Employer Contribution - Increase Amount and Total Contributions
FY 06 - 07 - 08 - 09
(in Millions of Dollars)

Fiscal Year	State of Alaska		University of Alaska		School Districts		Municipalities		Total All Categories	
	Increase	Total	Increase	Total	Increase	Total	Increase	Total	Increase	Total
FY 06	40.0	142.1	7.8	26.3	38.6	151.5	21.7	66.6	108.1	386.5
FY 07	41.5	188.9	8.0	35.2	39.7	195.2	22.5	91.6	111.7	510.9
FY 08	43.0	238.9	8.3	44.8	41.0	242.6	23.3	118.4	115.6	644.7
FY 09	8.9	257.1	3.4	49.8	31.4	282.1	4.7	127.6	48.4	716.6

Notes: Conformed to the 2004 Actuarial Valuation (using June 30, 2003 financial statements), by projection year
5% a year increase in employer composite rate until required computed total rate is reached.
Each subsequent year affected by change in rate, increase in salaries -

V02
14-Oct-04
11:01 AM
Division of Retirement & Benefits



State of Alaska

Projections Under Different Economic Scenarios – Key Assumptions

All assumptions and methods are the same except:

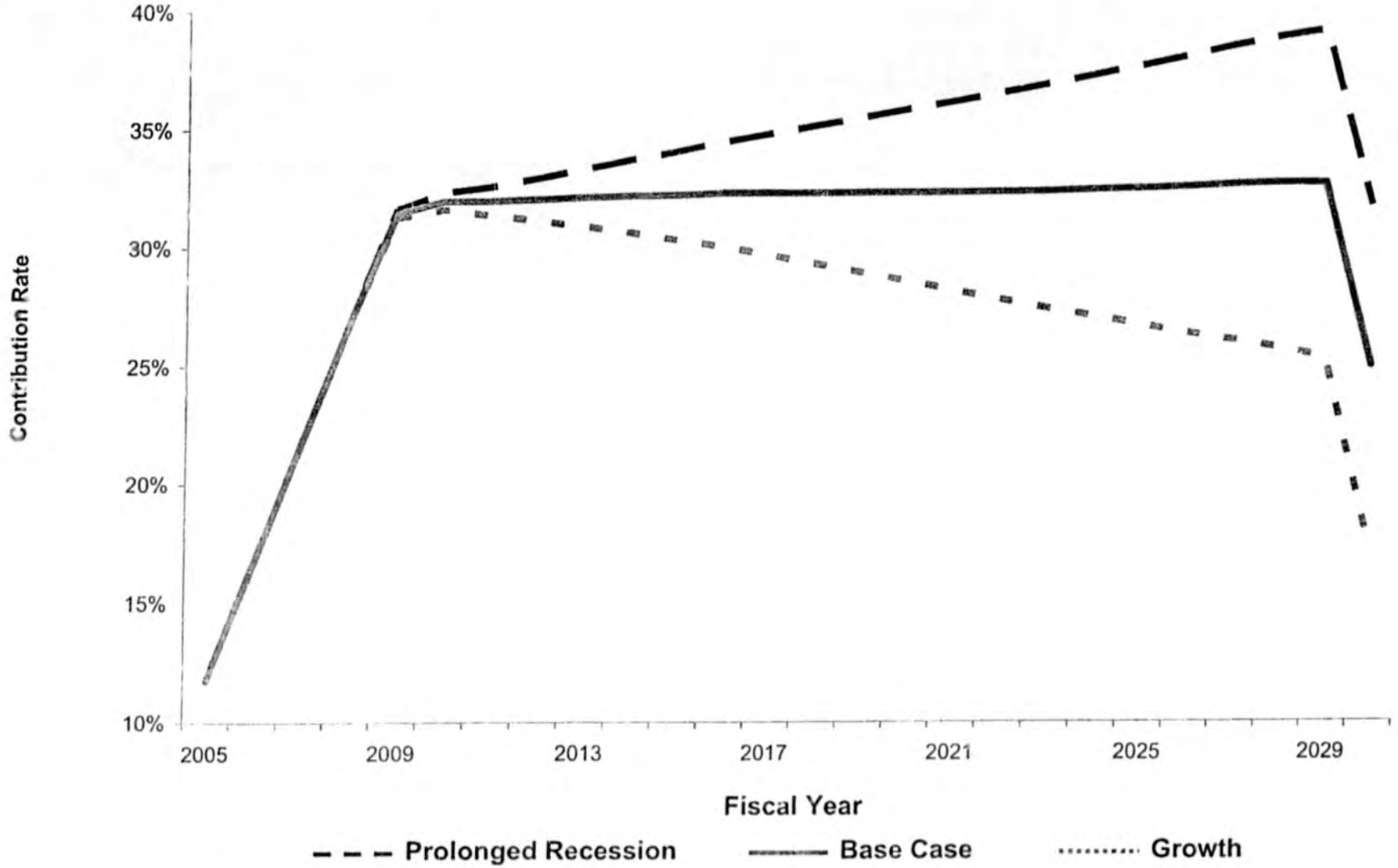
- Results are shown only under the 1% population growth scenario
- The actuarially calculated contribution rate is adopted in each year, but rate increases are assumed to not exceed 5%
- Investment returns are assumed as follows:

Total Portfolio Investment Return Under Each Scenario:

Base Case:	8.25% for all future years
Optimistic:	9.00% for all future years
Pessimistic:	7.50% for all future years

State of Alaska - PERS

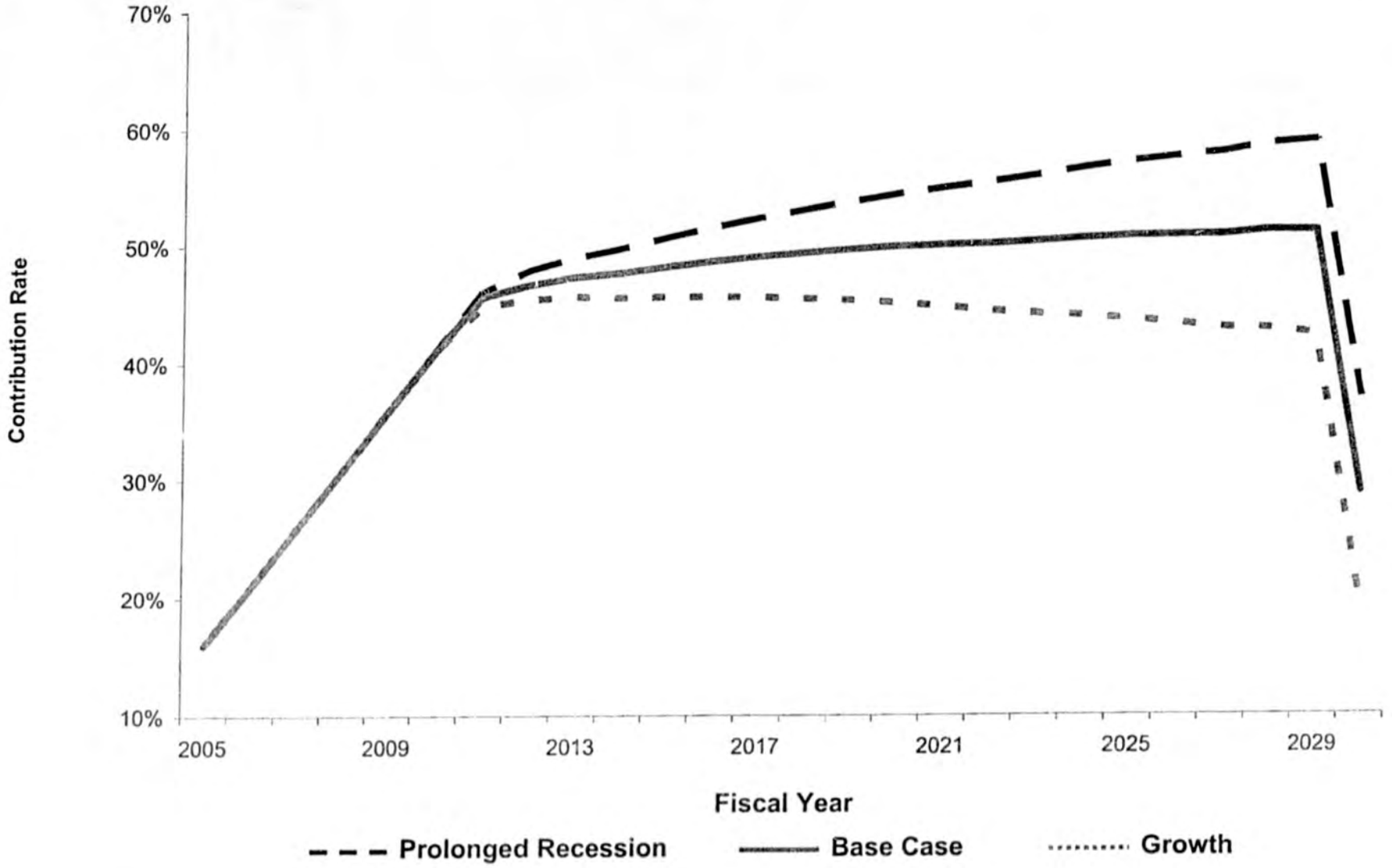
Economic Scenarios – Projected Contribution Rates
Annual Population Increase 1%



Mercer Human Resource Consulting

State of Alaska - TRS

Economic Scenarios – Projected Contribution Rates
Annual Population Increase 1%



Mercer Human Resource Consulting

Hypothetical Effect of Changes in Liabilities and Assets

Hypothetical Increase in Calculated Rate

	PERS	TRS
5% liability increase	3.40%	4.70%
5% market asset decrease	0.30%	0.50%

Liability changes may affect both normal cost and accrued liabilities

Asset changes are "smoothed" twice

- gains and losses are recognized over 5 years
- change in unfunded is then amortized over 25 years

Asset changes increase rates for 4 more years

- cumulative effect is 5 times first year effect

STATE OF ALASKA

DEPARTMENT OF ADMINISTRATION

DIVISION OF RETIREMENT AND BENEFITS

FRANK H. MURKOWSKI, GOVERNOR

PO BOX 110203
JUNEAU, AK 99811-0203
TDD: (907) 465-2805
FAX: (907) 465-3086
PHONE: (907) 465-4460
TOLL-FREE 1-800-821-2251

AUG 2 6 2005

August 24, 2005

The Honorable Bruce Weyhrauch, Chair
Special Committee on Ways and Means
House of Representatives
State Capitol, Room 421
Juneau, Alaska 99801-1182

Re: Follow-up From Special Ways and Means Meeting on July 14, 2005

Dear Representative Weyhrauch:

This letter is written in response to questions raised and requests made by members of the Special Committee of Ways and Means during the meeting on July 14, 2005. As a consequence of the time constraints during the meeting, I was not able to expand on several of the topics raised and wanted to take this opportunity to provide the members with some supplemental information as outlined below.

2002 Actuarial Audit of PERS / TRS – Milliman USA

Enclosed is a copy of the actuarial audit report prepared by Mark Johnson, F.S.A, Consulting Actuary with Milliman USA dated October 24, 2002, as requested by Representative Rokeberg. It is important to note that in addition to the actuarial valuation reports that are provided to the legislature annually in accordance with existing statute provisions that SB 141 prescribes additional reporting functions by the Alaska Retirement Management Board to the legislature.

For example, Section 141 of the bill states that the Alaska Retirement Management Board shall provide a report to the legislature by the 15th day after the first regular legislative session that includes: (1) preliminary assessment of the financial health of all public employees' retirement plans and all teachers' retirement plans; (2) assessment of the actuarial services purchased by the board; (3) recommendations for additional legislative or administrative policy to improve the financial health of the retirement plans; (4) short-term and long-term recommendations for addressing the unfunded

liability of the retirement plans; and (5) recommendations for legislative procedures regarding fiscal notes for new legislation affecting retirement plans.

Regulation 2 AAC 35.900 – Maximum Employer Contribution Rate Change

This regulation for PERS states that the maximum change in the contribution rate for an employer from one year to the next shall be no more than five percentage points, as actuarially calculated, whether the change is an increase or a decrease. The regulation was established at the request of Municipality of Anchorage (MOA) for budgetary purposes on May 17, 1991. Representative Wilson had raised concerns about this regulation during the meeting. This regulation is schedule to be repealed as part of SB 141.

AS 39.35.475 and AS 14.25.143 - Ad Hoc PRPA and Automatic (PRPA)

There are two versions of Post Retirement Pension Adjustment found in the above statutes. The ad hoc PRPA is based on the change in the cost of living in the Consumer Price Index (CPI) for Anchorage. Only Tier 1 members of PERS and TRS are eligible for the ad hoc PRPA, which is based on the financial condition of the retirement systems and is therefore discretionary. The amount of the ad hoc PRPA will not exceed four percent compounded for each full year in which benefits have been received. Because the ad hoc is discretionary the system does not pre-fund for this benefit.

As I mentioned during the meeting, the Commissioner of Administration has not approved an ad hoc PRPA for the last three consecutive years (2003, 2004, and 2005). Additionally, SB 141 recognized the significant cost associated with this benefit, which represents $400 million of the unfunded liability over the last ten years. As a result, SB 141 requires that the systems' funding ratio be at 105 percent before an ad hoc PRPA can be granted in the future.

Additionally, as part of Tier II legislation for PERS and TRS members the legislature enacted an automatic PRPA. This benefit is available to retirees who are age 60 and over and those who have received benefits for 5 years. The automatic PRPA is 50 percent or 75 percent (for members who are age 65) of the cost of living increase from the prior year as identified in the Anchorage Consumer Price Index (CPI). This benefit is pre-funded through employer contribution rates.

Actuarial Services RFP

The Division has released an RFP for actuarial services. The schedule to award a contract for actuarial services to the successful bidder is October 1, 2005. It

is anticipated that the Division will receive bids from multiple nationally recognized actuarial firms that specialize in government sector pension plans.

Actuarial Valuation 2005

It was mentioned during the hearing that a valuation for PERS and TRS should be conducted as soon as possible. Actuarial valuations are conducted on the PERS and TRS on an annual basis. The schedule has been for the Division to send the data to the actuary after the payroll records can be verified and confirmed for the period ending June 30, 2005. This information is normally sent to the actuary in September in order to produce a valuation for Board review and adoption. The valuation process from beginning to end takes approximately six to seven months. After the Board adopts the valuations, it becomes final and is provided to the Governor and to the legislature.

The cost for a valuation for PERS and TRS is approximately $70,000. Based on RFP for actuarial services being sought, it appears this schedule can still be maintained.

Rising Medical Costs

A request was made by Representative Gruenberg about information related to rising medical costs. Specifically, he was interested to know why medical costs are rising. This request is being researched and will be provided once the research is completed.

Union Participation in New Tiers

A concern was raised during the meeting that the various Unions may not have had an opportunity to be actively involved in discussion about new Tiers. I wanted to provide background information to address this concern. In January of 2004, the Commissioner of Administration launched an initiative to have Board members from the Public Employees' Retirement System and the Teachers' Retirement System research and study the design of new Tiers.

As part of this process, several public meetings were held regarding new Tiers including a survey sent to 12 collective bargaining units in June of 2004. Additionally, two unions participated in several of the Tier Sub-committee meetings, which were NEA and RPEA, which represents Retired Public Employees' Association.

In closing, the Division is committed to assisting the Ways and Means Committee in their efforts to review the PERS and TRS matter. As mentioned

in earlier correspondence, it would be beneficial for the Division to receive information about the resource needs for the committee so that any additional costs are identified appropriately for budgetary purposes. Further, it would be beneficial to know if the Special Committee on Ways and Means will have inquiries of the Division's actuarial consultant or need additional work to be performed by the actuary.

Please let me know if you have any questions about this correspondence.

Sincerely,

Melanie Millhorn
Director

Enclosure (Executive Summary of Milliman USA audit)
cc: Members of Special Committee on Ways and Means

Ray Matiashowski, Commissioner
Department of Administration

Kevin Brooks, Deputy Commissioner
Department of Administration

State of Alaska

Actuarial Audit of TRS & PERS

October 24, 2002

Mark O. Johnson, F.S.A.
Consulting Actuary

A MILLIMAN GLOBAL FIRM

Milliman USA
Consultants and Actuaries

111 SW Fifth Avenue, Suite 2900
Portland, OR 97204-3690
Tel +1 503 227.0634
Fax +1 503 227.7956
www.milliman.com

October 24, 2002

Mr. Guy Bell, Director
Department of Administration
Division of Retirement and Benefits
333 Willoughby Ave., 6th Floor
Juneau, AK 99811

Re: 2002 Actuarial Audit of TRS & PERS

Dear Mr. Bell:

The enclosed report presents our findings and comments resulting from a detailed review of the actuarial services currently performed by your retained actuary, William M. Mercer, Inc. (Mercer). Milliman USA, Inc. was selected to perform this review following an RFP process completed in June of this year.

Our findings are categorized under two levels of significance to the overall financing of the Systems, and summarized in Section 1. More detailed commentary on our review process and suggested considerations for adjustments to actuarial assumptions or procedures are included in subsequent sections of this report.

We wish to express our appreciation for the cooperation provided to us by the Mercer consultants, you and your staff. We look forward to discussing our report with you and the two Boards of Trustees on October 24, 2002.

Sincerely,

Mark O. Johnson, F.S.A.
Consulting Actuary

Section 1

Summary of Recommendations

Purpose and Scope of the Actuarial Audit Review

The purpose of an actuarial audit is to review the work performed by the Systems' actuary to assure the actuarial condition of each System is accurately measured, and that the contribution rate, together with the current assets, is sufficient to provide the benefits promised to members. You need to have an opinion regarding the accuracy and reasonableness of the following:

- The reasonableness, consistency and accuracy of the method, factors, and assumptions used in the actuarial valuations,
- The reasonableness, consistency and accuracy of the compilation of the actuarial valuation, and
- The reasonableness, consistency and accuracy of the results and the actuarial assumptions generated from the experience study.

Our specific methodology for the actuarial audit services requested was discussed in our proposal. We have followed all of the steps outlined in the proposal

Performing an actuarial audit is similar to doing detective work. The auditing actuary is presented with a set of facts, the "clues", and then tries to reconstruct the past events based on the available data. The auditing actuary's information is never as complete or detailed as that available to the retained actuary. Nevertheless, the purpose of the audit is to have the auditing actuary acquire a certain level of confidence that the findings and the results of the retained actuary's work are reasonable and were performed according to generally accepted actuarial standards and principles.

Outstanding Issues

Over the next month, we will complete the following tasks:

- Review the individual employer rate calculations,
- Validate the accounting disclosures, and
- Suggest areas for improvements in the reporting of the findings.

We will be available, as requested, to answer questions about our reviews and provide additional comments as warranted.

Statement of Key Findings

Based upon a thorough review of the 2000 experience studies and the 2001 actuarial valuation reports, including the underlying data and calculations, we found the actuarial work to be generally reasonable. The valuations were performed in accordance with generally accepted actuarial standards and principles. However, we found a number of areas where changes are needed, and have additional observations and recommendations for improving the actuarial process.

This report includes a detailed discussion of all the elements of our review. The major issues are categorized under two levels of significance to the overall funding status of the Systems.

Level A Areas where changes are needed which will result in a financial impact on the actuarial findings. Because we did not perform a replication audit, we will only be able to offer a "broad-brush" directional analysis of the fiscal impact our findings.

Level B Areas where we recommend changes based on our professional opinions or preferences.

These issues are outlined on the following pages. Our observations and recommendations are discussed in later sections of the report in more detail.

Level A Findings

Areas where changes are needed which will result in a financial impact on the actuarial findings:

1. TRS: Salary data was collected for the year ending on the valuation date and was used without escalation in the first projected year after the valuation. The Actuarial Liability for active member pensions is understated by one-year's wage growth and merit salary scale.
   (understated liabilities)
2. PERS: Salary data was collected for the six-month period ending on the valuation date and was used without escalation in the first projected year after the valuation. The Actuarial Liability for active member pensions is understated by one-half-year's wage growth and merit salary scale.
   (understated liabilities)
3. TRS: The salaries for part-time members are not converted to the equivalent full-time rate to project retirement benefits.
   (understated liabilities)
4. TRS & PERS: The projected death benefits are calculated without the application of the joint & survivor factors.
   (overstated liabilities)
5. TRS & PERS: The projected disability benefits for currently active members do not include service beyond the normal retirement age.
   (understated liabilities)
6. PERS: P&F occupational disabilities are always projected at 66.67% of compensation.
   (overstated liabilities)
7. PERS: Alaska COLA is assumed to be payable to 71% of retired members for some valuation calculations, even though the last experience study reduced this assumption to 68% of retired members.
   (overstated liabilities)

We have discussed all of these technical issues with Mercer and they have indicated their concurrence with our findings. We understand Mercer is currently working on the fiscal impact of making the appropriate changes.

Level B Findings

Areas where we recommend changes based on our professional opinions or preferences:

8. TRS & PERS: We believe the entire set of methods should be reviewed as a package. A number of the methods in use are unusual and may not, under certain conditions, provide the level of conservatism or stability the Boards desire. We have alternative suggestions to consider for the actuarial cost method, the amortization strategies, and the asset valuation method.
9. TRS & PERS: We recommend the assumption for future medical cost increases be reviewed prior to every valuation. In addition, we recommend the starting point for future projections be pegged to the latest known blended premium rather than an adjusted previous level.
10. TRS & PERS: We recommend the merit salary scale be reviewed carefully with consideration for a graded schedule with higher increases in the early years of employment.
11. TRS: The valuation assumes one simplified set of early retirement reduction factors to predict early retirement benefits. We recommend that the actual factors be used in the valuation.
12. TRS & PERS: The valuation assumes the resident COLA is applied to the entire benefit, rather than only to the basic benefit.
13. PERS: The valuation determines which tier the active member belongs to. We recommend the Systems provide Mercer with a data code, if possible, that indicates each non-retired member's tier.
14. TRS & PERS: The census data provides insufficient detail for the actuary to accurately predict future retirement benefits for vested terminated members. We recommend that Mercer work with the Systems to develop an accrued benefit or improved information on pay and service histories.
15. The observation period for the Experience Studies should be at least four years, rather than the two-year period used in the latest studies.
16. The Experience Studies and the Actuarial Valuations should provide more depth of information. We will provide detailed suggestions in a later report.

Terry Harvey

From: Rep. Bruce Weyhrauch
Sent: Thursday, August 25, 2005 10:51 AM
To: 'Bruce Weyhrauch'
Cc: Ginny Austerman
Subject: FW: PERS & TRS returns

From: Tom H. Boutin [mailto:tom_boutin@revenue.state.ak.us]
Sent: Thursday, August 25, 2005 8:28 AM
To: Rep. Bruce Weyhrauch
Cc: Ginny Austerman
Subject: PERS & TRS returns

Representative Weyhrauch,

I think that some time ago you had asked me for the PERS & TRS FY05 investment returns. We received them this week.

Tom

Tom:

The investment returns for PERS and TRS for the fiscal year ended June 30, 2005 are 8.95% for the PERS and 9.01% for TRS.

Gary

cc Melanie Milhorn

NEA-ALASKA

Affiliated with the National Education Association

House Ways and Means Committee, Bill Bjork's Testimony

September 8, 2005

Good afternoon, Chairman Weyhrauch and members of the House Ways and Means committee. My name is Bill Bjork, I am the president of NEA-Alaska. NEA-Alaska represents more than 12,500 public school employees throughout Alaska. I would like to thank the committee for coming to Fairbanks and for taking their valuable time to have meetings around the state on the PERS and TRS issue.

I will focus on the scope of this meeting, and not dwell on the pitfalls and problems of the legislation passed during special session (Senate Bill 141).

NEA-Alaska believes the critical first step must be to define the problem accurately. Solutions CANNOT be determined until the magnitude of the problem is truly determined or since it is hunting season, do we need the howitzer or would a .22 suffice. Applying either the howitzer or the .22 in the wrong situation could have devastating effects.

We need an independent actuary to review the current retirement systems to determine what actuarial assumptions ought to be applied to the retirement systems.

Joseph Esuchanko, the independent actuary hired by the Legislative council to examine the PERS system, reported to the council that Mercer is using a methodology that only 11-16% of public systems utilize to determine liability of public pension systems. Please note the fact that the method being used leads to higher liability projections.

Before a "solution" can be crafted, agreement on the actuarial assumptions should be reached so that we can all agree on what solution to apply. Solutions CANNOT be determined until the magnitude of the problem is truly determined

Look closely at the actuarial assumptions:

It has been NEA-Alaska's request since May 2004, that the assumptions being used match the experience in Alaska.

Mercer's Assumptions	Alaska's Experience
Inflation will be 3.5%	2.6% over any ten year period; PF uses 3%.
Wage Growth 3.75-4.5%	1.36%
Investment return 8.25%	9% over any ten-year period
Health Care Costs 12.5% - 5%	8% (7.5% according to Esuchanko)

ANCHORAGE REGIONAL OFFICE • 4100 Spenard Road • Anchorage, Alaska 99517 • (907) 274-0536 • FAX: (907) 274-0551
JUNEAU OFFICE • 114 Second Street • Juneau, Alaska 99801 • (907) 586-3090 • FAX: (907) 586-2744
FAIRBANKS REGIONAL OFFICE • 2118 S. Cushman Street • Fairbanks, Alaska 99701 • (907) 456-4435 • FAX: (907) 456-2159

Assumptions attached to Alaska's reality could definitely lead to a different liability amount.

Inflation
If you address inflation, Mercer assumes a 3.5% inflation rate. Alaska's experience is 2.6% over any 10--year period in our state's 46-year history. The Alaska Permanent Fund, one of the most respected funds in the world, currently valued at over $31 Billion dollars, uses the more accepted 3% inflation figure. So what difference does a .5 percent make (the difference between 3.5% and 3%)? Over 20 years it is $800 million dollars! Over 30 years, to match retirement eligibility, it is well over a billion dollars!

Wage Growth
Mercer uses a 3.75 to 4.5% figure, our members wish this was true! Since 1989 Alaska teacher salaries have grown by 1.36% per year with the largest growth in the past seventeen years, the 3.23% increase this past year. The erroneous assumption on wage growth has a huge impact on the unfunded liability.

Investment Return
The Alaska State Pension Investment Board has accomplished a rate of return in excess of the actuarial assumptions over every 10-year period.

Medical Care Costs
Mercer predicts current annual increases in excess of 12% tapering off in 2014 to annual increases of 5%. NEA-Alaska's experience is 8% annual increases in the immediate future continuing beyond 2014. Joseph Esuchanko recommended projecting 7.5% annual increases.

The assumptions used by the actuary who helps this committee define the magnitude of the retirement system shortfall ought to be inline with Alaska reality.

The Ways and Means Committee will need additional information about the current retirement systems to accurately define the shortfall.

Liability Associated With Each Tier in TRS and PERS
Common sense suggests the benefits provided by tier 1 of both PERS and TRS produce the majority of the liability. If you separate the tiers and calculate past service costs independently for each tier, is there still liability in the PERS tier 3 and TRS tier 2 retirement packages? This information is critical to assist the committee in defining the shortfall.

Medical Costs
NEA-Alaska believes that a huge portion of the projected liability rests in skyrocketing medical costs. The medical care program currently in place ought to be better managed. The NEA-Alaska Health Trust provides medical coverage for 13,000 people currently. The Trust knows how to manage care and consistently "beats the market" in rate increases. Medical costs are a key to the shortfall and

richly deserve the attention of this committee.

Process Recommendations

NEA-Alaska strongly recommends the state retain an independent actuary. Advice provided by Mercer brought Alaska's retirement system from over funded three years ago to a liability of about $5.7 billion today! We can't revise the current system until we have confidence that the actuarial assumptions are valid.

Indeed, NEA-Alaska believes the State should research whether Mercer owns part of the liability.

A final recommendation would be a request that a group of stakeholders be brought together to review and analyze data provided by an independent actuary. This analysis would assist the Ways & Means committee on a final work product.

Again I appreciate the opportunity to provide this testimony. NEA-Alaska and our members look forward to future opportunities to participate.

TESTIMONY of
Sam Trivette, President
Retired Public Employees of Alaska
HOUSE WAYS AND MEANS COMMITTEE
September 8, 2005

- Please review my written testimony to the Committee of July 14, 2005, in which I give my background on PERS/TRS issues; explain "what got us where we are today"; and make recommendations for examining and correcting problems with our retirement system. It is clear that SB 141 did NOT fix many of the problems that caused the pension under funding nor did it take a hard look at the assumptions on which SB 141 was based.

- Mercer Consulting was employed by the state to provide actuarial information used in the drafting of SB 141. Mercer's actuarial calculation methods are only used by about 11% of the actuaries nationally; therefore I would urge that you hire a different actuarial firm that uses a more common method for calculating actuarial information and have that firm review Alaska's data prepared by a different firm.

- Most legislators understand there are basically two components of the retiree plans, the pension component and the medical benefits component. The pension component is well funded, over 100%. It is the health care component that has contributed to under funding of PERS/TRS. Costs of health care are skyrocketing throughout the United States. It is a problem for public employees, private employees, Medicare, Medicaid, and all who fund these systems. It is NOT unique to public retiree systems. In Alaska health care costs are at least 25% higher than the "lower 48", according to a recent article in the Anchorage Daily News.

- Retirees don't control the costs of health care, but they have voluntarily taken strong action to reduce their health care costs in recent years by RPEA working cooperatively with the PERS/TRS Boards, the health care administrator (Alaska Care), and Retirement and Benefits. Six million Dollars a year is saved annually by the cooperative effort of the retirees, PERS/TRS Boards, and Alaska Care to educate the retirees that everyone benefits by using generic drugs.

- At the last joint PERS/TRS health subcommittee meeting in April 2005, a number of additional ideas were brought forth that could result in significant savings to the cost of the retiree health care system if implemented. Experience has shown repeatedly it is only through the combined cooperative efforts of all the parties these savings will come to pass. And typically a dollar spent on education returns two dollars in savings. The Alaska Constitution guarantees retiree benefits, but plans can be changed and costs reduced if we work with and educate our retirees.

- SB 141 eliminated the PERS/TRS Boards. Some type of advisory board to the new ARM Board involving retirees will be necessary if you hope to achieve the magnitude of savings the PERS/TRS Boards working cooperatively were able to achieve. RPEA is willing to work with you to draft such legislation. This joint effort is critical for containing the costs of medical expenses, a key to increasing the solvency of the retiree trust funds. Working together we can improve upon SB 141 to save retiree trust fund money. A healthy Alaska retiree trust fund benefits all Alaskans.

- Oversight of retiree trust fund money is also important for three programs that are complete self funded by retirees; the Long Term Care Program, the Life Insurance Program, and the Dental, Audio and Visual Insurance Program. I'll gladly provide additional details if you wish.

- The only potential solution to the PERS/TRS under funding I heard mentioned anytime during Senate hearings on SB 141 was Pension Obligation Bonds. After listening to the expert testimony at your July 14 hearing, doing my own subsequent reading and discussing it with some financial experts, I strongly oppose this solution. At this point, I see no other viable option but a general fund appropriation, once you have the additional actuarial analysis done and you have a more definite understanding of the status of the fund. Remember the fund has rarely been close to 100% funded over the last two decades.

Terry Harvey

From: Rep. Bruce Weyhrauch
Sent: Thursday, August 25, 2005 10:51 AM
To: 'Bruce Weyhrauch'
Cc: Ginny Austerman
Subject: FW: PERS & TRS returns

From: Tom H. Boutin [mailto:tom_boutin@revenue.state.ak.us]
Sent: Thursday, August 25, 2005 8:28 AM
To: Rep. Bruce Weyhrauch
Cc: Ginny Austerman
Subject: PERS & TRS returns

Representative Weyhrauch,

I think that some time ago you had asked me for the PERS & TRS FY05 investment returns. We received them this week.

Tom

Tom:

The investment returns for PERS and TRS for the fiscal year ended June 30, 2005 are 8.95% for the PERS and 9.01% for TRS.

Gary

cc Melanie Milhorn

Dorothy Thompson
P.O. Box 80368
Fairbanks, Alaska 99708
(907) 479-6712

Dear Representative Weyhrauch,

Re: Restore Retirement Funding

My husband and I are both retirees under PERS. We are disappointed and concerned that SB141 does nothing to fix the deficit in retirees' and Present employees' retirement. The deficit in funding is still just as it was before passage of this flawed legislation.

Further legeslative audeting, as proposed by Rep. Mike Kelly, just diverts attention but does nothing to resolve this urgent deficit problem.

Please act to restore funding for our retirement.

Sincerely,

Dorothy Thompson

Testimony on PERS/TRS Funding Short Fall 9-8-05 / Ways & Means Committee

I'm Doris Robbins, retired from Alaska Department of Labor, and a member of the Retired Public Employees of Alaska. Thank you for the opportunity to voice my opinion.

You should have my written testimony in your packet. It is a rather harsh attempt to get your attention, because I feel I and all retirees have been ignored to this point.

We were told all during session that SB 141 legislation would fix the deficit in both retirees' and current employees' retirement funds. It does not do that. The same deficit is there, so we are now attending these hearings on how to fix it.

Rep. Kelly's News-Miner letter yesterday suggested an audit to find out what happened to the money. That would have been a good idea had it come before he helped get SB 141 passed. Normally, the legislature investigates a problem first, legislation is drafted to fix it AND THEN there is an analysis of the bill. After that it goes through the process of passage. That did not happen.

So now we are going to back track to fix a funding short fall similar to that of other states across the country. The old retirement system could have been tweaked, such as was suggested by several different actuarial opinions. The money could be repaid over a long period of time so it would be less of a burden. Any time you replace a system, you incur extra costs just to get the new one going so you have added to the problem.

What I know is that the employment contract I agreed upon is binding. It is the State of Alaska's responsibility to fix the problem because it was state action which allowed it to get so bad.

The PERS/TRS board advised the Administration to be more conservative during the stock market boom, particularly with Baby Boomers coming. The board even hired a second opinion actuary which confirmed their opinion. They were still ignored, as they only have the power to advise.

The Dept. of Administration, the Governor, and the legislature put into law the practices which led to the problem. I acknowledge there was one of those boom to bust periods for which the stock market is famous and the repayment should be dealt with similar to what other states are doing.

I hope you will now look seriously at the facts and work on the problem in a bipartisan manner. There have been some good ideas advanced already. Please go back and look at them. It isn't too late! Don't forget about the cost of health care, which is the largest culprit. You have been given ideas on lowering costs there as well.

Thank you for giving me and other retires an opportunity to be heard.

Doris Robbins *Doris Robbins*

Doris Robbins
3763 Mitchell Avenue B
Fairbanks AK 99709
(907) 374-0597

Ginny Austerman

From: Dorothy Thompson [reddot@acsalaska.net]
Sent: Thursday, September 08, 2005 11:36 AM
To: Ginny Austerman
Subject: Restore Retirement Funding

Dear Representative Weyhrauch,

My husband and I are both retirees under PERS. We are disappointed and concerned that SB141 does nothing to fix the deficit in the retirees' and present employees' retirement. The deficit in funding is still just as it was before passaage of this flawed legislation.

Further legislative auditing, as proposed by Rep. Mike Kelly, just diverts attention but does nothing to resolve this urgent deficit problelm.

Please act to restore funding for our retirement.

Sincerely,
Dorothy H. Thompson
P.O.Box 80368
Fairbanks, Alaska 99708
(907)479-6712

Ginny Austerman

From: Karen Steen [steen@mtaonline.net]
Sent: Thursday, September 08, 2005 10:06 AM
To: Ginny Austerman
Subject: SB141 Teleconference

I am unable to attend the teleconference and express my opinions, so am sending this email.

There are a lot of problems created by this legislation. I don't believe it is in the states best interests to institute this change, but my interests' center on how it effects my retirement. The State contracted for my services, took my money to fund a retirement with certain benefits, including appeals methods, a cost of living allowance and income until I die. I put in my time in good faith. The state can't arbitrarily change the contract.

If this legislation is allowed to stand without correcting the injustices, I can see nothing but law suits into the foreseeable future. This state doesn't need that expense. Fix the problems or rescind the legislation.

THX Nicholas Steen
HC 32 Box 6561
Wasilla, Alaska 99654
(907) 745-2739

Ginny Austerman

From: Steve Porter [srp13ak1@yahoo.com]
Sent: Thursday, September 08, 2005 9:06 AM
To: Ginny Austerman
Subject: PERS

I request that you add my comments to the record of the hearing scheduled for today, September 8, 2005. I am a retired State employee. The changes to the retirement system will result in high transition costs, as well as increased costs to manage the individual private accounts of the new defined contribution plan. In addition, after July 2006 there will be no new members contributing to the PERS system I retired under which only increases the long term viability of the fund. SBS 141 did not fix anything, it only made the "claimed" under funded liability worse. Instead of destroying a proven pension system that provides a modest retirement income to public employees and then increasing costs to the State with a new retirement system, the Legislature should fix the problems in PERS. A few adjustments would be far less costly than the new defined contribution plan.

Stephen R. Porter
700 Cedar Street
Anchorage, AK 99501
907/522-0349

Steve

Click here to donate to the Hurricane Katrina relief effort.

Ginny Austerman

From: Lois Conway [loisc@mtaonline.net]
Sent: Thursday, September 08, 2005 8:58 AM
To: Ginny Austerman
Subject: PERS/TERS Funds

Whatever you do to make it happen, you must make good your commitment to retirees. That is all I have to say. It is the law.

Lois Conway
P. O. Box 94
Palmer, AK 99645
907-746-0424

Ginny Austerman

From: Michelle Decker [mhd@gci.net]
Sent: Wednesday, September 07, 2005 10:34 PM
To: Ginny Austerman
Subject: Testimony re SB 141

I will keep this short and sweet:

- The above legislation does not correct the problem of the PERS/TRS Retirement Fund as claimed by legislators who pushed it and voted for it. On the contrary, this legislation will ultimately cause MORE underfunding of the system.

- The long-term effects of this legislation will not only cause significant harm to public employees, but to the general public in a trickle-down effect. Legislators are doing this to gain votes now for themselves--the public employees and the future of the state economy be damned.

- There were and are many superior ways to address the underfunding issue and there has been testimony already to that effect. I urge legislators to show some real leadership and statesmanship by stopping this train before it crashes. The public throughout the nation is getting truly fed up with legislators misrepresenting facts for self-serving reasons. It's time to admit that SB 141 was/is a mistake. It's time to apply all the sound suggestions already made for fixing the system, not destroying it, only to be replaced by a seriously flawed system that creates more serious problems. We all know the saying, "The cure is worse than the disease."

Michelle H. Decker
7766 Port Orford Drive
Anchorage, AK 99507

Ginny Austerman

From: Frank Abegg [frankabegg@acsalaska.net]
Sent: Wednesday, September 07, 2005 8:29 PM
To: Ginny Austerman
Subject: *****SPAM***** PERS/TRS Retirement Hearing

I am writing this email to you since I cannot attend tomorrow's teleconference on the State Pension program. I want to go on record of being very concerned with the changes the State of Alaska is making in the State Retirement program. It is not the pension member's fault that the State mismanaged the pension fund and even allowed abuse by some to seriously impact its economic viability. The State is responsible for maintaining our retirement funds. The Administration has always had the final word on managing these accounts. The PERS/TRS Board only acted as advisors to the State in the past. We have held up our end of the deal. It is the responsibility of the State to fix this problem.

Section 112 of the bill makes it impossible for current retirees to earn a cost of living adjustment. The language permits the increase only when the ratio of total fund assets to the accrued liability meets or exceeds 105%. By SB141 removing all future employees – some 5,000 each year – from PERS and TRS, there will be no new money into the system, exasperating the unfunded liability. The liability will only grow larger and further strain the system. The State needs to solve the pension fund's financial deficit, not reduce pension benefits on its participants.

The PERS/TRS pension programs are based on contracts with its employees, who have held up their end of the deal by paying their assigned share as defined by the State. The State needs to ensure that fair and equitable treatment will continue for its pensioners. I also predict that removing pension member representation from the Pension Board may become a major issue in the future if fair treatment of appeals and continued level of the pension benefits is not ensured by the Administration. I trust that the State will maintain its contractual promises to its retirees.

Frank Abegg
PERS Retiree
3512 Ida Lane
Fairbanks, AK. 99709
907-479-3431

Ginny Austerman

From: GRileyH@aol.com
Sent: Wednesday, September 07, 2005 8:00 PM
To: Ginny Austerman
Subject: 141

Don't mess around with my retirement. My wife and I don't have many years left, but we are entitled to retirement increases and health insurance coverage. Election time is not too far off. M aybe we need people in the Senate who care.

G. H. Riley
1918 Parkview Circle
Anchorage, AK 99501
(907) 276-3334

Ginny Austerman

From: GRileyH@aol.com
Sent: Wednesday, September 07, 2005 7:58 PM
To: Ginny Austerman
Subject: SB 141

As a retiree under the PERS system, I was promised pay increases to my retirement pay as well as health insurance coverage for life. That is what the State of Alaska should be doing. Having new people come into the system will shore it up. Please leave what "works" along.

Peggy Riley
1918 Parkview Circle
Anchorage, AK 99501
(907) 276-3334

Ginny Austerman

From: Elisabeth Christensen [franziska@gci.net]
Sent: Wednesday, September 07, 2005 6:53 PM
To: Ginny Austerman
Subject: SB 141

I do not like SB 141 for the following reasons: (1) It will not correct the underfunding which was not caused by the employees. (2) It leaves future employees unprotected for the remainder of their lives if they care to stay in Alaska. SB 141needs to be reversed.

Elisabeth R Christensen
PO Box 190744
(Residence) 8741 Kathleen Dr
Anchorage AK 99519
Phone: 907-243-1578
e-mail address: franziska@gci.net

Ginny Austerman

From: Oliver & Andrea Backlund [kestrels@acsalaska.net]
Sent: Wednesday, September 07, 2005 5:42 PM
To: Ginny Austerman
Subject: TRS/PERS funding issue

Please include my comments for consideration by the legislature.

As a former state employee (I worked for the University for 17 years and retired under one of the several RIP programs) I find it difficult to credit the sincerity of the legislature or the executive branch when you claim that there is a crisis in the funding of the retirement program.

After all, the legislature was fully aware that you were asking people to leave their jobs so that presumably cheaper and younger persons could take them. Presumably you were aware that if we retired earlier, we would likely live long enough to draw all if not more than the amounts we had deposited in the system. You or your predecessors created this problem, we simply accepted your offer, assuming that you had made it in good faith. It would be a betrayal of those men and women who have worked for Alaska and helped to build its roads, communities and University for you to change the system from a defined benefits to the defined contribution one proposed. For one thing, this proposal creates a two-class employment system. For another, the defined benefits option relieves the State of its obligation to protect its present and former employees against the exigencies of the market and the economy. How convenient for you, and how full of portent for those who have given you and this state their best years.

Andrea Backlund

P.O. Box 82349

Fairbanks, Alaska 99708

907-479-2632

Ginny Austerman

From: Oliver & Andrea Backlund [kestrels@acsalaska.net]
Sent: Wednesday, September 07, 2005 5:29 PM
To: Ginny Austerman
Subject: PERS/TRS Teleconference on Juderfunding

Do not break faith with present retirees or present public employees whose retirement plans have been carefully planned in advance. Restore funding for retirement.

Oliver Backlund

P.O. Box 82349

Fairbanks, Alaska 99708

907-479-2632

Ginny Austerman

From: Colleen Nicholson [whitedog@aptalaska.net]
Sent: Wednesday, September 07, 2005 3:17 PM
To: Ginny Austerman
Subject: SB141

I am a retired public employee and closely followed all the sessions last spring concerning the Stedman sponsored bill to change the structure of our retirement system including taking away all representation of the members of PERS/TRS boards and changing from a defined benefit system to defined contribution. We were left with the impression that the bill would also "fix" the fund shortfall in the process. Now I learn that it not the case and I believe this administration has played fast and loose with those who trusted your integrity. Now I believe that not only your integrity is in question, but that we have been lied to by "words", that reliable counsel has been ignored, and that we are victims of a dishonest administration.

Colleen Nicholson
Retired Municipal employee
401 Fram Street
Petersburg, AK 99833 Resident of Alaska continuosly since 1944.

Ginny Austerman

From: Spencer [conook38@alaska.net]
Sent: Wednesday, September 07, 2005 3:16 PM
To: Ginny Austerman
Subject: SB141

To Whom it May Concern:
Please include my opinion in your offerings to the legislature concerning SB 141. We NEED to overturn this legislation that will effect my retirment/health care and that of my children who are also teachers. They have contributed under the "old" plan but will not be able to retire with a secure income/healthcare because of this bill.

Judith DeVito
340 Thompson Place
Kenai AK 99611

907-283-7437

Ginny Austerman

From: Gene and Phyllis [epbartels@gci.net]
Sent: Wednesday, September 07, 2005 9:47 AM
To: Ginny Austerman
Subject: Audit of PERS and TRS funds

Please restore the funding for our retirement. Please restore having retiree representation on the Board.

Please answer the question of how the shortfall happened by doing the audit of the fund. Thank you.

Eugene and Phyllis Bartels

Retired PERS employees

1110 Hoselton Road

Fairbanks, AK 99709

907\479-0434

Ginny Austerman

From: Rep. Bruce Weyhrauch
Sent: Wednesday, September 07, 2005 9:20 AM
To: 'Bruce Weyhrauch'
Cc: Ginny Austerman
Subject: FW: My Retirement Funds

-----Original Message-----
From: tmhelm@ptialaska.net [mailto:tmhelm@ptialaska.net]
Sent: Tuesday, September 06, 2005 7:14 PM
To: Rep. Bruce Weyhrauch
Subject: My Retirement Funds

Email For: Representative Bruce Weyhrauch
From: tmhelm@ptialaska.net
Name: Myra Jane Helmer
Street: 2331 Nussbaumer St
City: Fairbanks, AK
Zip Code: 99706

Subject: My Retirement Funds

Dear Sir,
I may not be able to attend the meeting on Thursday at 1:00, but I want to be heard about any \'odd\' withdrawals from the Teacher\'s Retirement Fund. That should not be touched by any of the State\'s other funds that are suffering.
Please stand firm. Thanks so much,
Myra Helmer

Ginny Austerman

From: Darwin Walter [darwal@gci.net]
Sent: Tuesday, September 06, 2005 12:35 AM
To: Ginny Austerman
Subject: SB 141

"BS"141 (SB141) solves nothing. It needs to be ammended to provide for defined benefits and real strategies for addressing the shortfall. Penurious Republican philosophies have dire future results...witness the unnecessarily disastrous results of hurricane Katrina. Pennies saved today costs millions of dollars tomorrow.

Ginny Austerman

From: Doris Robbins [drobbins@gci.net]
Sent: Monday, September 05, 2005 9:30 PM
To: Ginny Austerman
Subject: [Fwd: Fw: RPEA ** Call to Action ** 9/8/05 PERS/TRS Teleconference - Group 2]

-------- Original Message --------
Subject: Fw: RPEA ** Call to Action ** 9/8/05 PERS/TRS Teleconference - Group 2
Date: Mon, 05 Sep 2005 20:53:00 -0800
From: Carolyn Tuovinen <tuovinen@gci.net>
To:"ZZZ Robbins, Doris" <drobbins@gci.net>
CC:AA Carol Earnhart <carolea@attglobal.net>

----- Original Message -----
From: Lila
To: Carolyn Tuovinen
Sent: Saturday, September 03, 2005 2:14 PM
Subject: Re: RPEA ** Call to Action ** 9/8/05 PERS/TRS Teleconference - Group 2

I cannot be at the teleconference Thursday. Here are my thoughts on this.

I think it is up to the state to cover the shortfall in the retirement fund. The state contracted with their employees at retirement time to manage the fund to cover their retirement payments. They seem to find money to cover anything they want - they can cover this shortfall.

Lila Fergus
840 Rockside Road
Wasilla, AK 99654
907-376-6907

Ginny Austerman

From: Dave Hamilton [dlh0@hotmail.com]
Sent: Monday, September 05, 2005 9:26 PM
To: Ginny Austerman
Subject: PERS Situation...

Please restore funding fro our retirement. The actions taken to date are overly-drastic and heavy handed. I fullfilled my part of the deal by serving a term of service and retired with 25 years state time. I feel a fully funded retirement system is not only possible for the state of Alaska, but a duty and responsibility, as well.

Thank you,

Dave Hamilton
Fairbanks

Ginny Austerman

From: Connie Janzen [lonestarconnie@gvec.net]
Sent: Monday, September 05, 2005 3:01 PM
To: Ginny Austerman
Subject: vote for funding shortfall

Please count my vote for "**Restore funding for our Retirement**" per the RPEA & PERS & TRS RETIREES funding shortfall.

Thank You

Dieter Janzen
279 Gustav Ln
San Marcos, TX 78666

(830) 379-1944

Ginny Austerman

From: terryruthmc@comcast.net
Sent: Monday, September 05, 2005 11:04 AM
To: Ginny Austerman
Subject: Retirement funding

Please register my protest at the proposed cutting of retirement funding. Iin this time of record oil revenue income it is inconceivable that the legislature would even consider reneging on the State's committment to its retirees. Please restore the funding to our retirement accounts.

Terry McFadden

Ginny Austerman

From: glenna dunlevy [gbdunlevy@gci.net]
Sent: Monday, September 05, 2005 10:59 AM
To: Ginny Austerman
Subject: state retiree hearings

5 sept 2005 thank you very much for holding hearings on the state retiree system. i really having a hard time living on my retirement because of rising medical costs. i was forced into retirement by my employer because of a fall that resulted in a broken wrist. after 13 years work and no down time i receive a pension of 347.00 dollars. i find it very hard even with social security to make ends meet. again thank you for having the hearings so that all the voices can be heard. i am sure i am not the only one striving to make ends meet these days. yours truly. glenna dunlevy

Ginny Austerman

From: Terry or Cindy Luther [tcluther@gci.net]
Sent: Monday, September 05, 2005 9:58 AM
To: Ginny Austerman
Cc: Carolyn Tuovinen
Subject: Whose fault is it anyway?

Hello Ginny,

I am a State retiree as of two years ago. I worked for Division of Forestry as a SR19 Pilot II and wildfire suppression specialist. I was Nationally Certified and was the first State pilot awarded that national distinction. It has been said that my direct initial efforts in newly discovered wildfires resulted in over 25 million acres of saved timberland over my ten years in this job. This both in Alaska and Outside. I bet other State employees have done even more. I feel that the Governor's office does not consider little things like this from it's State employees....or care about them.

I can't tell you how angry it makes me to see the State messing around with band aids like SB 141 which does not really address the problem at all. The unfunded liability here is the doing of our Legislature and other hig level planners and it seems they were asleep at the wheel! Now we employees will be asked to suffer for it. The present system works, albeit not perfectly, so lets fix it properly.

So far our Governor has ignored everyone and bought himself a airplane and terminated the Seniors Bonus program....and now this!

I'm a lifelong Republican but you know what? Whatch me in the next election....and I'm going to watch every elected officials vote on this issue too.

Our State employees are a wonderful group of dedicated people who DON'T make too much money or get too many benefits. We should take care of them rather than create an adversarial position against them. Our next big move is a general strike as is presently pending with TRS employees.

Terry Luther
Anchorage

Ginny Austerman

From: Marguerite Stetson [ffmas@aurora.uaf.edu]
Sent: Sunday, September 04, 2005 11:45 AM
To: Ginny Austerman
Subject: Restore funding for our retirement...

I would urge that you restore funding for the state retirement system.
This is especially important in order to attract new teachers to the educational system throughout Alaska. Alaska no longer has the highest pay for teachers.

Thank you for your consideration.

Marguerite Stetson
3009 Northwood Street
Anchorage, AK 99517

Ginny Austerman

From: brenda martin [gypsyroadqueen2000@yahoo.com]
Sent: Sunday, September 04, 2005 11:22 AM
To: Ginny Austerman
Subject: restoring funds to our retirement system

We are out of state and unable to attend the meeting in Fairbanks but would like our voices to be heard. My husband and I are both retired teachers and are extremely concerned about the underfunding of PERS/TRS. Both systems are good systems when they are funded fully. Please restore the funds to our retirement system.

Sincerely,

Brenda and Ron Martin

Do You Yahoo!?
Tired of spam? Yahoo! Mail has the best spam protection around
http://mail.yahoo.com

Ginny Austerman

From: MARGUERITE STETSON [mstetson1@verizon.net]
Sent: Sunday, September 04, 2005 7:46 AM
To: Ginny Austerman
Cc: lebmrich@gci.net
Subject: Please restore funding for our retirement!

As a retired teacher, I am very concerned about the future of education in Alaska if we do not have an adequate plan for retirement for these teachers. We are no longer the state paying our teachers the highest salary.

Marguerite Stetson
3009 Northwood Street
Anchorage, AK 99517

Ginny Austerman

From: Raymond E. Nelson [renelson@gci.net]
Sent: Saturday, September 03, 2005 2:14 PM
To: Ginny Austerman
Subject: SB-141 (for Teleconference Sep 8, 2005

To Whom it May Concern:

As a Municipality of Anchorage retiree under the PERS program, I would like to comment on SB-141 as being in opposition to this solution to the problem of retirement funding. As I, personally, will not be affected by this legislation, my comments are made free of self-interest.

There are many other possible fixes and cost-cutting opportunities available to the Legislature rather than the draconian steps that have been taken. To many and well know to mention here, these have all been brought up before the Legislature in past years but nothing was ever done. Certainly the progran needs a thorough overhauling and clean-up. Taking this action and putting into place the several other fixes which correct, rather than destroy, the retirement program would have gone a long way toward cutting cuts and restoring viability.

Instead, it seems to me that the Legislature, rather than fixing the various problems in program, has decided to take the opportunity to dump the program altogether, using the so-called threat to the Permanent Fund as the means of enabling the plan. (These days it appears that the perfect way to obtain public support for any dubious project is to say that not doing so will threaten or destroy the Permanent Fund, and the public, not be well-informed on the subject, acquiese, understandably wishing to protect the Fund).

In this case, if the PERS program were completely overhauled, the errors and loopholes fixed, and various adjustments made, in other words the things done that the Legislature has refused to do over the last several years, the program could be saved without threatening the Permanent Fund in any significant way.

I know that personally, without the PERS program, the checks I receive every month and the health care benefits I have, my retirement would be a rather grim and bleak experience. Certainly the quality and dedication of the Municpal and State employees of the future will decline as their compensation packages decline. Can Alaska, as a State wherein government by necessity plays such a large part in its economic development, really afford the probable mediocraty in its employees?

Surely there is a better outcome possible here, so that people of good will and a Legislature willing to shoulder its proper responsibilities can come to a common understanding that works for everybody, the employees, the Government and, as a result, the people of the State of Alaska.

Sincerely,

Raymond E. Nelson
Member: RPEA
MOA Retired

renelson@gci.net

Ginny Austerman

From: IFEllison@aol.com
Sent: Saturday, September 03, 2005 1:02 PM
To: Ginny Austerman
Subject: RETIREMENT FUNDING

RESTORE FUNDING FOR OUR RETIREMENT!!!

Ginny Austerman

From: rsamsal@aol.com
Sent: Saturday, September 03, 2005 12:27 PM
To: Ginny Austerman
Subject: *****SPAM***** Retirement Fund Shortfall

To: House Ways and Means Committee
From: judysamsal@cox.net

I am a state retiree writing from Oklahoma where we have moved from Alaska. We are here because of decisions that are made by our government. The decisions made by elected government officials affect the lives of every day people in a big way.

We are here because one of our daughters is in Florida, within driving distance from here, having been stationed there with her husband, who is in the military and is subject to being sent to Iraq. He is often away from home on assignment in locations other than Iraq. They were blessed with triplets three years ago, and the babies are now three years old. However, they are in a position to be without a father, and last year alone, there were five hurricanes which narrowly missed them. Hurricane Katrina, which just hit the Gulf Coast, was, at one point, headed for Florida. We are here so we don?t have to fly for 11 hours (if there are any airlines left in business) to get to them in case of a catastrophe, and so one of us can be there in their father?s absence. We are also helping with our grandchildren who live in Oklahoma because our economy is such that their mother has to have a full time job. For one thing, their father?s overtime has been cut, and now he?s working long hours for no extra compensation which complicates the daycare situation, not only in paying for it, but in getting the children picked up on time. Now, with the price of gasoline cutting into their salaries even further, young families are having extreme hardship making ends meet. We are just happy to be able to help with the children and have a part in their lives. I?m not complaining about the children.

This federal administration and frankly, the Alaskan state government, are already creating a grim climate of hardship, and are moving the middle class into poverty and I don?t see how it is going better until these people are gone. I would think with oil in the $60 ? 70 dollar a barrel range, the State of Alaska would somehow find a way to keep their commitments. I hear they have money to spend on luxury jets that have little to do with the enforcement of state laws, and are funneling money into their own pockets. If the government spent as much effort creating good living conditions for the country (which is the job they signed on to do) as they do at feathering their own nests, we might all be in better shape and not just the super wealthy getting wealthier. PLEASE fund our shortfall.

Ginny Austerman

From: Linda Hull [lhull1942@yahoo.com]
Sent: Saturday, September 03, 2005 12:24 PM
To: Ginny Austerman
Subject: *****SPAM***** PERS AND TRS FUNDING

I JUST WANT TO GO ON RECORD ALONG WITH MY HUSBAND WHO IS A PERS PERSON. WE NEED YOU TO FUND OUR RETIREMENT. WE WORKED IN SOME QUITE AMAZING PLACES DOING AMAZING THINGS, BUT WE STUCK IT OUT, AND WE NOW NEED YOUR SUPPORT TO CONTINUE TO MAKE OUR RETIREMENT POSSIBLE. THANK YOU FOR YOUR HELP. LINDA HULL AND LOWELL HULL, 2181 TWIN FLOWER DRIVE, FAIRBANKS, ALASKA 99709.

Do You Yahoo!?
Tired of spam? Yahoo! Mail has the best spam protection around
http://mail.yahoo.com

Ginny Austerman

From: Donald Frost [frostyak@hotmail.com]
Sent: Saturday, September 03, 2005 12:20 PM
To: Ginny Austerman
Subject: Re: teleconference

Ginny, I am writing in support of RPEA's attempt to influence the legislature in regards to thier changing the retirement system without thoroughly examining other alternatives.

I support RPEA's efforts.

Donald W. Frost retired

Ginny Austerman

From: Stewarts [stewart2642@gci.net]
Sent: Saturday, September 03, 2005 11:48 AM
To: Ginny Austerman
Subject: *****SPAM***** RPEA Member

Please restore funding for or retirement!

Sharon Stewart
19361 Upper Skyline Drive
Eagle River, AK 99577
907-694-2642

Ginny Austerman

From: Norma Bowkett [bowkett@cox.net]
Sent: Saturday, September 03, 2005 9:53 AM
To: Ginny Austerman
Subject: PERS/TRS Funding Shortfall

(For Rep. Bruce Weyhrauch, Chairman, House Ways and Means Committee)

In the interest of quality education for Alaska's youth, we urge you to restore funding for the retirement system.

Sincerely,

Gerald E. Bowkett and Norma S. Bowkett, members, Teachers Retirement System

14604 W Horizon Drive
Sun City West, AZ 85375
(623) 214-7665
bowkett@cox.net

--
No virus found in this outgoing message.
Checked by AVG Anti-Virus.
Version: 7.0.344 / Virus Database: 267.10.18/89 - Release Date: 9/2/2005

Ginny Austerman

From: Pat Corbin [sumfunow@alaska.net]
Sent: Saturday, September 03, 2005 7:26 AM
To: Ginny Austerman
Subject: PERS/TERS

It is unbelievable to me that this oil rich State of Alaska is about to 'crush' the futures of the many, many, loyal, hardworking people who do so much of the work of the State, and keep our 'ball rolling'!! How does this legislature think we are to "grow this economy" and keep the valuable people who make this a great place to live if they pull out the most valued reason the people keep 'pressing on'?! The SB 141 promoters have their priorities and values terribly out of place.

Funding *must be* returned to the retirement of the people who 'carry the load'!

Patricia Corbin.....an extremely dismayed and appalled citizen and voter!

Ginny Austerman

From: rsamsal@aol.com
Sent: Saturday, September 03, 2005 7:20 AM
To: Ginny Austerman
Subject: *****SPAM***** Retired Retirement Bennifits

Dear House and Ways Committee Members:

Please restore funding for our State of Alaska retirement. Since retirement we depend on the money to live on. We moved out of state to help raise our grandkids.

Ronald Samsal
10909 Windmill farms Road
Midwest City, OK 73130
e-mail rsamsal@aol.com

Ginny Austerman

From: Dave and Molly Brann [brann@alaska.net]
Sent: Friday, September 02, 2005 10:43 PM
To: Ginny Austerman
Subject: Pers/Ters

To the Legislature,
I strongly feel that there should be no shortage of funds for the Pers/Ters retirement program. If there is a shortage of funds, it must be because the legislature "borrowed" from Pers/Ters funds in the past.

This is a problem that needs to be solved even if the legislature needs to allocate funds to Pers/Ters from the general fund. Please look at this problem again and find a way to provide the funds that have been promised to Pers/Ters retirement programs.

Thank you,
Molly Brann
PO Box 1901
Homer, AK 99603
907 235 6018

Ginny Austerman

From: Bev's Mail [mytern@gci.net]
Sent: Friday, September 02, 2005 9:08 PM
To: Ginny Austerman
Subject: SB 141

I am a state retiree, and do not wish to have any benefit changes.....as it would affect my living in Alaska during my retirement. I worked for the state for many years.....and the only reason I stayed with a state job was the benefits. It was certainly not the pay. We were underpaid, but the benefits were good.

There are too many people already affected by Gov. Murkowski's methods with the longevity program. Nobody could afford to live here in this great state if our benefits are reduced by any amount.

Please do not touch the retirees benefits.

Bev.

Ginny Austerman

From: Irene A. Jacobson [iaj@gci.net]
Sent: Friday, September 02, 2005 8:50 PM
To: Ginny Austerman
Subject: My testimony

I agree with other retirees! Please count me in!
Thank you!

I. A. Jacobson

Sing a New Song
Ps. 81:1

Ginny Austerman

From: R & D Wells [wellsbad@chartermi.net]
Sent: Friday, September 02, 2005 11:19 AM
To: Ginny Austerman
Subject: Ways and Means Committee Testimony

My name is Dorothy Wells. Although I am presently living in Michigan, I lived for forty years in North Pole, taught my entire teaching career at Eielson, served 21 years on the TRS board, and the last 12 years on ASPIB -- Alaska really is home. I speak for myself.

Thank you, Representative Weyhrauch, for conducting these hearings. I am sorry this process wasn't followed BEFORE SB 141 was passed. My comments will cover four areas.

1. Although SB 141 is law, and you are presently trying to deal with the funding issue, I have to say that I am very sorry that our very rich state passed such legislation changing a good DB plan to a DC plan. It makes reliable retirement planning nearly impossible. Having said that, I think that once you get good cost information, you will learn that Tier 3 in the PERS system actually costs the employer less than the new DC plan will cost. Further, since the DB plan will go on for at least 70 years more, the funding for that plan will become more and more expensive. Defined benefit plans are funded on the basis of perpetuity, with an unending supply of new people coming into the plan, and with a LONG time horizon, thus allowing investments to ride out economic cycles. That will become more and more impossible as there are fewer and fewer people paying into the system.

2. Since Mercer and Ms. Milhorn testified and gave much of the information before passage of this bill, I think it incumbent on this committee to seek additional information elsewhere now. There are several people in the state who were involved with the retirement systems much longer than Ms. Milhorn has been -- Anselm Stack and Guy Bell to name two. It would be enlightening to get their input.

3. The configuration of the new ARM board concerns me. ASPIB has worked VERY well with eight trustees -- I don't believe there has ever been a four to four vote on anything, thus the even number of trustees has not been an issue in getting business done. Further, PERS and TRS members have a lot of their own money in the retirement systems, and should be able to vote for their trustees instead of having them be governor appointments. The nine member board, all governor appointees, sends out the message that this is a very political board, controlled by the governor, and I don't think that's the message we want to send to state employees.

4. While I disapprove of the entire bill, I do need to point out that teachers are REALLY disadvantaged with this bill in that they are not part of SBS, nor are they covered by Social Security.

Thanks for letting me testify.

add to record

Hon. Representative Bruce Weyhrauch
House Ways and Means Committee
State Capital Room 421
Juneau AK 99801-1182

RE: PERS/TERS Funding Shortfall
Date: September 8, 2005

Summary of Testimony of Charles H. Gallagher, State of Alaska Retiree

I am submitting for your consideration a paper I wrote for myself after I retired in 2002. I wrote the paper before the issues before this committee became apparent. I wrote this paper because, as an auditor I needed to try and understand my pension and retirement finances.
It shows the State of Alaska in effect used my contributions and theoretically their obligations to my PERS retirement account well before I got to use them.

Under the Windfall Elimination Provisions of the Social Security Act in the early 1980's the State of Alaska was allowed to withdraw from participation. That also meant it withdrew me and my spouse from a substantial amount of participation in Social Security benefits. That needs to be remembered in these deliberations.
The legislature established the Supplement Benefits System. By the simple comparison of the two systems, PERS and SBS, one can see the enormous effect of the nation's financial expansion in the 1990s. In a nutshell it appears my interest at PERS grew at 2.3% while the SBS at times was growing at 18%.

This could be regarded as gross mismanagement, or as an odd Ponzi scheme. In effect it allowed our various governments to spend those monies elsewhere deferring their responsibilities for another day.
Thus in a way the public has already had a certain financial relief. It just happened during the past decade. Now it is time to return the funding and the opportunity is fortunately at hand through enormously high oil prices.
Thank you for offering me this opportunity to be heard.

PAY: Analysis for 25 years

When I was hired by the State of Alaska it was not my intent to make money, nor had I taken the job for a career. I took the job because there nothing else to do. Having been through several Fairbanks recessions I knew things could get tough, here at the end of the road. When there were no jobs, there were no jobs, and there was no nearby place to go. I took the job because I wanted to stay in Fairbanks. I knew I could earn a living, but no one ever thinks about a government job being lucrative. The times and circumstances in Alaska were to make my job quite worthwhile, but it was due to luck and some good decisions.

My pay as an adjudicator, investigator and auditor was enough to squeeze by on as there were benefits. The State Government increases one's pay based upon a merit system; however, the merit system was never actually based on merit, but upon longevity. I never heard of a merit increase not being granted. If it was not, the logic was that it would be contested by the union. Pay increased incrementally by steps toward a journey level after about fifteen years unlike the standard four or five years as in most occupations. My job paid just below the published average for an auditor when I attained my full merit increases.

Soon after I began work in 1977 Alaska State income tax was eliminated. That single item meant an increase in expendable income in itself for all Alaskans.

The pension is the Public Employees Retirement System -PERS. The pension plan offered when I started was relatively standard despite the constant griping from the public and legislature. It is no Cadillac of a plan. The record shows about a 6% contribution by me each pay period. It paid a constant 2.3% interest for 25 years. During many of those same years the Standard and Poor Index Fund was averaging 18%. The fund was reaping the theoretical 16% difference on my personal contributions, but not to my account. Tenure was achieved at five years.
The Employer supposedly matched my contributions. However, the Employer's (State's) theoretical contribution never showed up on the balance sheet. By Law I was entitled to the plan I began permanent employment under in March 1977.

This pension alone would not have allowed me to retire at 55. It entitled me to about $28,000.00 per year. That is poverty level for a family of four.

What made the difference was the State's leaving the Social Security System in 1982. This was allowed because of the provisions for separation of Federal and State power in the Constitution, Article 11. The change coincided with the beginning of the greatest economic expansion in U.S. history. Former Social Security contributions by the Employer and Employee went into the Supplemental Benefit Retirement System -SBS. As with the pension plan the contribution was about 6%. Both Employer and Employee contributions were accounted for by a regular statement. Contributions could be invested at the Employee's direction depending upon personal risk.
Our contributions expanded exponentially with the national expansion. At one point our employment condition was described as the "Golden Handcuffs". One was simply increasing their retirement more than they were being paid. One could not afford to leave work without forfeiting future potentials.
One did need to know when and where to manage their money/risk. Investments in low risk funds yielded little. Future recessions could risk higher risk funds. I was in an index fund, and the expansion covered most minor setbacks. In November 1998 I had left the markets for shelter in Money Markets. I knew from 30 years experience on Wall Street whenever every Tom, Dick, and Harry gets in, it is time to get out. I had made a lot. On 5-9-2001 I left the Market with my SBS at about 11,000 on the Dow Jones. I felt it was too risky. It was the third high on a backside of the market. I moved to treasury notes, the markets contracted into recession soon afterwards.
As the pipeline oil flow decreased from two million barrels per day to one, the legislature modified the State Employee pension plans three times since 7-1-77 in attempts to come to grips with State budgets. After 7-1-77 the calculations of the pensions eliminated leave cash-outs for new employees. In 1986 Legislative changes subsequently hit first the minimum age to retire and some benefits. Again in the mid-1990s another change increased retirement age to 65 and benefits were essentially eliminated. Somewhere in the mix tenure increased from five to ten years.

Ginny Austerman

From: Don & Carolyn Gray [dcgray@mosquitonet.com]
Sent: Friday, September 09, 2005 5:27 PM
To: Ginny Austerman
Subject: Re: David Teal's handouts from yesterday

Hi Ginny, Thank you for the David Teal handouts.
Also, I am attaching my written testimony since some of the legislators were out of the room when my turn came to speak and I would like for them to have it for the record.

Thanks,

Don

Don I. Gray
399 Hillside Drive
Fairbanks, AK 99712
(907) 457-5737 home
(907 322-3408 cell

Here is the testimony I gave to the Alaska House Ways and Means Committee Thursday afternoon:

" My name is Don Gray and I am a 35 year resident of Fairbanks.
Because of SB141, new public service employees in PERS and TRS in the defined contribution plan will no longer contribute to the pool of funds for earlier retirees, but the employers, (State of Alaska, boroughs, cities and local school districts) still have the obligations previously agreed upon in contract for the two retirement systems.

Earlier, Director David Teal of the Division of Legislative Finance described the advantage of paying down the unfunded long-term liability sooner rather than later as reducing the pain on school districts and municipalities in particular. This also reduces the pain on local taxpayers. The Director of the Division of Retirement and Benefits today told us that the actuary has recommended that employer contribution rates must increase 5% annually until they reach 28.19% for PERS and 41.78% for TRS and then remain at that level for approximately twenty-five years.
This 5% annual contribution increase, in and of itself, creates a cash-flow problem for many PERS and TRS employers, who in turn must turn to their local taxpayers for revenue.

Paying down the unfunded liability by the state now is, in effect, a form of municipal revenue sharing, with the exception that in this case the Legislature can direct that public money is spent as intended to reduce the liability and is not simply a windfall to any municipality Money is
fungible, so spending in one part of a budget permits saving in another part. As Director Teal indicated, it is pay now or pay later. If you postpone state payments, local taxpayers will feel directly the additional annual 5% increased employer contribution rates.

It is fairer if the State prepays unfunded pension liabilities and eliminates increased local employer contributions since this benefits communities in organized boroughs who would otherwise have to fund shortfalls from local taxes while other employers are funded entirely from state and federal sources and not from local taxes.

I urge you to pay down the unfunded long-term liability sooner rather than later. Debt is not our friend. "

==========

On Sep 9, 2005, at 11:59 AM, Ginny Austerman wrote:

> Some of you might not need this information, but sending to all at once saves me lots of time.
>
> Ginny
>
> > Ginny
> >
> > <Ways_Means_Committee_Packet_1.PDF>

North Slope Borough School District

September 8, 2005

Representative Weyhrauch, Chair
House Ways and Means
State of Alaska
Juneau, Ak 99801

First of all I would like to thank you for the long hours and hard work that has been put into SB141.

Today I would like to speak on the issue of how the current PERS/TRS increases affect our District – as it directly relates to delivering education.

According to a presentation made by a Mercer Human Resource Consulting representative to a joint PERS and TRS Retirement Board Meeting March 24, 2004, the PERS employer rate should be increased from then 11.77 % to 25.63% and the TRS employer rate should be raised from 16% to 38.85% to meet the needs.

Increases have been approved by the PERS and TRS Boards for FY05 and FY06, 5% and 5% respectively, and will likely be forthcoming for each of the next several years in an attempt to make the retirement systems financially sound. The Alaska Retirement Management Board is scheduled to set the FY07 rates at their upcoming meeting. The incremental impact of such a plan for the North Slope Borough School District (NSBSD), assuming the same number of staff each year, is estimated to be:

		TRS	PERS	Total Increase
Increase	FY06	$644,594	$614,567	$1,259,161
Increase	FY07	722,000	530,000	1,252,000
Increase	FY08	723,600	532,650	1,256,250
Increase	FY09	727,180	535,313	1,262,493
Increase	FY10	730,854	537,989	1,268,843
		$3,548,228	$2,750,519	$6,298,747

To put such increases into perspective for NSBSD, it could equate to the annual elimination of approximately 12-15 teaching positions if additional revenue is not forthcoming. Please bear in mind that the impact of the incremental rates for NSBSD for FY07 is over $1.2 million dollars. This increase alone is estimated to require $190 additional base student allocation.

P.O. Box 169 • Barrow, Alaska 99723 • Phone: (907) 852-5311

Has the Alaska Teachers' Retirement System and the Public Employee Retirement System been an important element in attracting and keeping capable employees – absolutely! These systems were put in place during a time that Alaska was struggling to attract a qualified teaching pool, of which a large percent came from 'outside'. A large percent still are hired from other states, however, we are beginning to grow our own from our University system.

Once again, thank you for your work in education as well as shoring up our current retirement systems and making the new system palatable.

LUCIENNE E. SMITH
Director of Business Affairs

LES/

Ginny Austerman

From: LIO Ketchikan
Sent: Thursday, September 15, 2005 1:53 PM
To: Ginny Austerman
Subject: RE: 9/8 W & M hearing head count

Hello. The only person in attendance was Miles Baker - staff to Sen. Stedman. Thanks, Cherene

---

From: Ginny Austerman
Sent: Thursday, September 15, 2005 1:38 PM
To: LIO Ketchikan
Subject: FW: 9/8 W & M hearing head count

Hi, can you please give me the breakdown, same as I requested below.

Thanks, Ginny

From: Ginny Austerman
Sent: Thursday, September 15, 2005 1:35 PM
To: LIO Kenai; LIO Homer
Subject: 9/8 W & M hearing head count

Hi guys,

Can I get a head count from you on the 9/8 W & M hearing, please?

Legislators #, Public #

Thanks,

Ginny

Ginny Austerman
Legislative Aide to Representative Bruce Weyhrauch
Committee Aide/ House Ways & Means Committee
Room 421 State Capitol
(907) 465-6863 (direct)
(907) 465-2273 (fax)

Ginny Austerman

From: LIO Mat-Su
Sent: Thursday, September 15, 2005 11:44 AM
To: Ginny Austerman
Subject: RE: 9/8 W & M hearing

Ginny,
Rep. Carl Gatto was the only one present and there was no public participants.
~Julie Dickerson
Matsu LIO

From: Ginny Austerman
Sent: Thursday, September 15, 2005 11:42 AM
To: LIO Mat-Su
Subject: 9/8 W & M hearing

Hi:

Can you please tell me how many people were at your location for the Ways and Means hearing last week. Legislators #, and public #.

Thanks, Ginny

Ginny Austerman
Legislative Aide to Representative Bruce Weyhrauch
Committee Aide/ House Ways & Means Committee
Room 421 State Capitol
(907) 465-6863 (direct)
(907) 465-2273 (fax)

Mat-Su 1
Kodiak 0
HOMER
FAI
ANC.
KENAI 1

[9/15/2005 1:17 PM]

Meeting Information Report
For the Period from 9/8/2005 to 9/8/2005

Meeting ID: 4926
Meeting Name: HWAM

Organizer: Lori Yorba
Contact: Lori Yorba
Billing Code: HWAM

	Scheduled	Actual
Date of Meeting:	09/08/05	09/08/05
Start time of Meeting:	01:00 PM	12:48 PM
Participants:	21	44
Length (minutes):	180	237
Total recording minutes:		202

Peak Number of Participants in meeting	26
Number of profile accesses to recording :	0
Number of guest accesses to recording:	0
Number of MeetingTime accesses to recording:	0

Attendees (includes those invited + those attended):

User ID	Time in Meeting: Voice	Workstation	Data Conference
Anch School Dist	191 min	0 min	0 min
Anchorage LIO1	191 min	0 min	210 min
Anchorage TC	0 min	0 min	0 min
Barrow Schedule	0 min	0 min	45 min
BobDoll	6 min	0 min	0 min
BonnieCheney	169 min	0 min	0 min
Charise/Kohring	86 min	0 min	0 min
ChrisE.	103 min	0 min	0 min
DaveDonaldson	98 min	0 min	0 min
David Teal	0 min	0 min	0 min
Erica	28 min	0 min	0 min
Fairbanks LIO	0 min	0 min	0 min
Fairbanks LIO2	190 min	0 min	215 min
Fairbanks Schedule	0 min	0 min	38 min
Guest User	1 min	0 min	0 min
HeatherBrakes	186 min	0 min	0 min
Homer LIO	190 min	0 min	0 min
Homer Schedule	0 min	0 min	202 min

Ginny -
This is the last of our system. Hope it helps.
Tes

[9/15/2005 1:17 PM]

Meeting Information Report
For the Period from 9/8/2005 to 9/8/2005

Meeting ID: 4926
Meeting Name: HWAM

Organizer: Lori Yorba
Contact: Lori Yorba
Billing Code: HWAM

	Scheduled	Actual
Date of Meeting:	09/08/05	09/08/05
Start time of Meeting:	01:00 PM	12:48 PM
Participants:	21	44
Length (minutes):	180	237
Total recording minutes:		202

Peak Number of Participants in meeting	26
Number of profile accesses to recording :	0
Number of guest accesses to recording:	0
Number of MeetingTime accesses to recording:	0

Attendees (includes those invited + those attended):

User ID	Time in Meeting: Voice	Workstation	Data Conference
JerryBurnett/Rev	186 min	0 min	0 min
Joe/Seekins	137 min	0 min	0 min
JoeEsuchanko	190 min	0 min	0 min
Kenai LIO	194 min	0 min	200 min
Ketchikan LIO	0 min	0 min	201 min
Ketchikan LIO	188 min	0 min	0 min
KevinBrooks	50 min	0 min	0 min
Kodiak Schedule	0 min	0 min	116 min
Kotzebue Schedule	0 min	0 min	45 min
LindseySovde	78 min	0 min	0 min
Lori Yorba	0 min	0 min	0 min
MarkPrussing	36 min	0 min	0 min
Matsu LIO	187 min	0 min	0 min
Matsu Schedule	0 min	0 min	201 min
Melanie Millhorn	0 min	0 min	0 min
MikeOhare/Kott	116 min	0 min	0 min
Nome Schedule	0 min	0 min	93 min
Peg Warren	0 min	0 min	111 min

[9/15/2005 1:17 PM]

Meeting Information Report
For the Period from 9/8/2005 to 9/8/2005

Meeting ID: 4926
Meeting Name: HWAM

Organizer: Lori Yorba
Contact: Lori Yorba
Billing Code: HWAM

	Scheduled	Actual
Date of Meeting:	09/08/05	09/08/05
Start time of Meeting:	01:00 PM	12:48 PM
Participants:	21	44
Length (minutes):	180	237
Total recording minutes:		202

Peak Number of Participants in meeting	26
Number of profile accesses to recording :	0
Number of guest accesses to recording:	0
Number of MeetingTime accesses to recording:	0

Attendees (includes those invited + those attended):

User ID	Time in Meeting: Voice	Workstation	Data Conference
Peg/Jnu	237 min	0 min	0 min
PegLIO	183 min	0 min	0 min
Rep Gruenberg	74 min	0 min	0 min
Rep Max Gruenberg	68 min	0 min	0 min
RepWilson	186 min	0 min	0 min
RichardDahlstrom	189 min	0 min	0 min
WaltonSmith	123 min	0 min	0 min
WaltonSmith/Y	53 min	0 min	0 min
chris eshleman/hom	88 min	0 min	0 min
markPrussing	28 min	0 min	0 min
mary lou elton	198 min	0 min	0 min
ted moninski	197 min	0 min	0 min
washingtondccaller	53 min	0 min	0 min

SITE: ANCHORAGE	SUBJECT OF MEETING or BILL #
COMMITTEE: HWAM	Review of PERS/TRS
DATE: 9-8-05	UPDATE #:

PRINT YOUR NAME	COMMUNITY	REPRESENTING/AFFILIATION	DO YOU WANT TESTIFY Y or N
Rep Rokeberg			Y
V. Kay Lahdenpera	Anchorage	Self	Y