

Public Employees' Retirement System (PERS)

Defined Benefit (DB) Plan

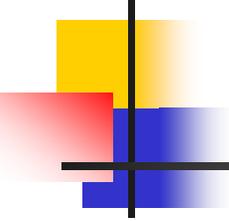
Accounting Issues

House Ways & Means

March 30, 2007

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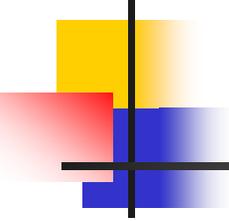




Why are we here today?

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

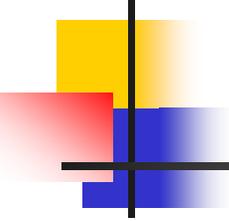




Proposed Solution

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





Proposed Solution (cont.)

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

PERS = One System (but Two Plans)

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



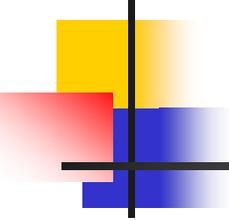
PERS DB

Accounting Issues

No impact on:

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

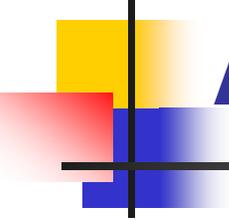




Agent Multiple Employer Plan

Defined and described as follows:

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

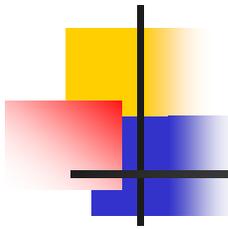


Alaska Statutes

AS 39.35.100 (b)(3)

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





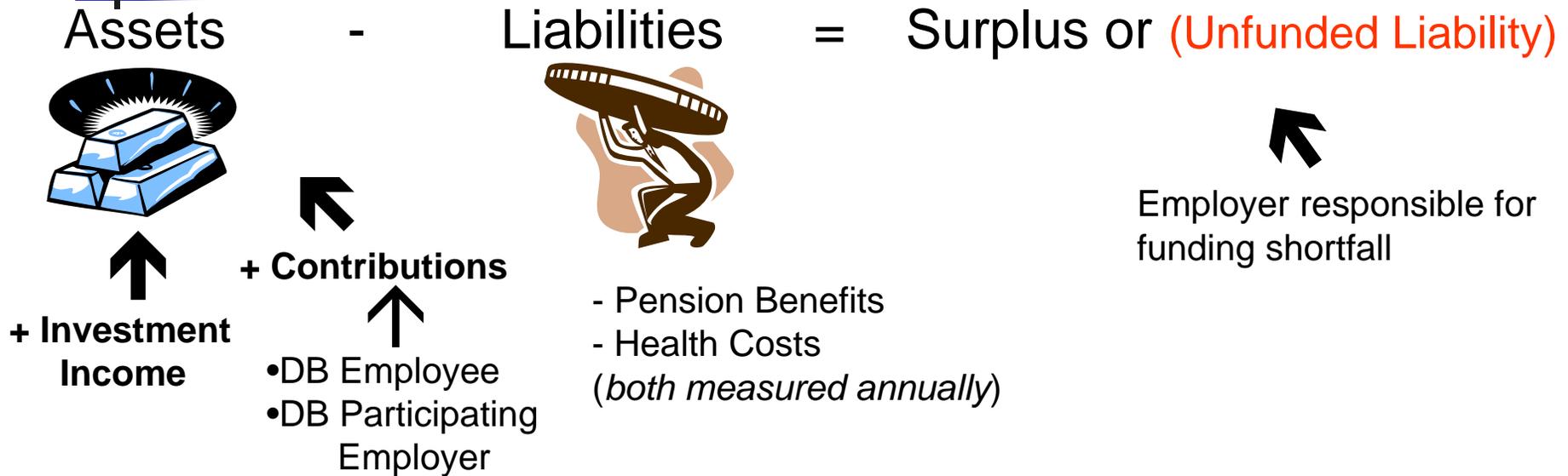
Alaska Statutes (cont'd)

- **AS 39.35.680 (22)** defines employee as “. . . a retired member. . .”

- **AS 39.35.250** states that the past service portion of the employer’s contribution rate is that “required to amortize the unfunded obligations of the employer. . .”

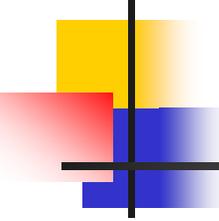


PERS DB Plan



- Calculation is performed at the employer level as well as at the plan level
- Concerns regarding employer level accounting and allocation methodologies in use

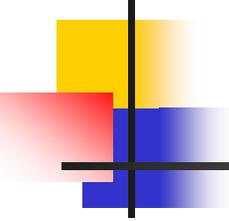




Assets

Employer contributions are accounted for in two separate buckets:

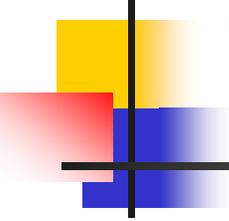
- Active employer asset accounts
 - One account for each individual employer
- Retiree reserve asset account
 - One consolidated account for all participating employers



Retiree Reserve Account

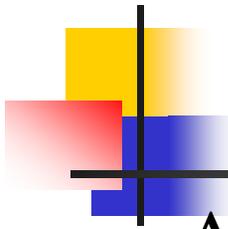
Funding Sources

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



Transfers

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



Allocation Process

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

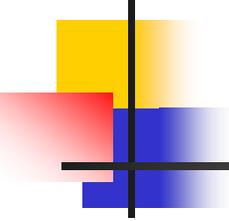
Allocation Example

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

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

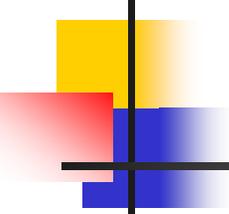
- Unfunded liability is \$112,353
- Employer has no retirees at 6/30/2004, so has not contributed to the retiree reserve account





Next Year – FY05

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



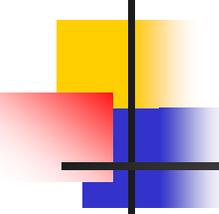
Allocation

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

Even though employer has not contributed to this account

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

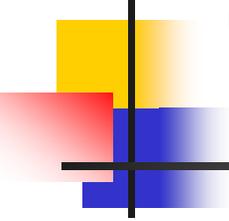




Transfer

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

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



Transfer

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

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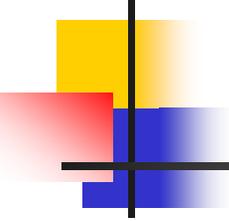
Effect of Allocation and Transfer

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

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

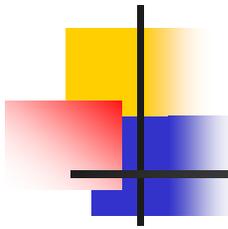
■ Over funded by \$192,428.





Liabilities

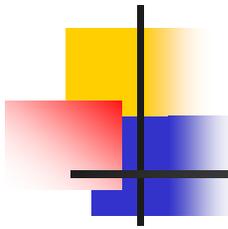
- Annually calculated by employee
 - Allocated to individual employer
 - Based on pro rata service earned with employer
 - Does not take into account salary earned with employer
 - Concerns have been raised about this allocation process as well



Liability Allocation Example

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

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



Example (cont.)

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

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

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



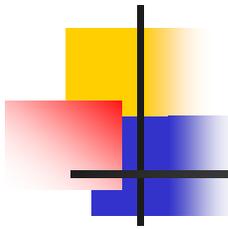
Impact on Contribution Rates

Assets - Liabilities = Surplus or
(Unfunded Liability)



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

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



Proposed Solution

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

