Summary of Legislation: Public Employee Retirement System (PERS)

Summary

The Public Employee Retirement System (PERS) unfunded liability is financed through a combination of contributions from PERS employers of 22 percent of payroll and a state assistance payment for the remaining liability made by the State of Alaska. The proposed change to the PERS statutes will impact the State of Alaska as a PERS employer by lifting the 22 percent cap on the payroll contribution for the State of Alaska only. All other PERS and all TRS employers' rates will remain unchanged.

This will shift the state's share of the unfunded liability from the annual state assistance payment, which is typically funded 100% with unrestricted general fund (UGF) revenue, to agency payroll, where it can be spread across all fund sources. This change is anticipated to save an estimated $43 million in unrestricted general funds each year by shifting these costs to other fund sources; mostly federal.

Nothing in this proposal will change the retirement system, costs to other participating employers, or benefits to plan members.

What is the problem?

Alaska has two main public employee retirement systems: the Public Employee Retirement System (PERS), with 142 current participating public employers, and the Teachers Retirement System (TRS), with 56 participating employers.

In the early 2000s policymakers became aware that both systems were significantly underfunded as a result of market losses, actuarial errors, and accelerating health costs. Significant legislative reforms were enacted to change the way the pension systems operated and were financed.

The first, to control the increasing liability, was the elimination of the defined benefit plan and creation of a defined contribution plan for new public employees who started service after June 30, 2006.

The legislature also created the Alaska Retirement Management (ARM) Board to manage the retirement systems replacing the separate boards for each system. The ARM Board was tasked with setting employer contribution rates for PERS and TRS normal costs as well as past service liability. Initial rates proposed by the ARM Board were dramatic increases for employers – averaging 40 percent of payroll for PERS and 54 percent of payroll for TRS. Each employer was assessed a different rate based on actuarial assumptions and plan experience and for some the rate increased to more than 100 percent of their total payroll.

In 2007 and 2008, the legislature established a uniform rate of 22 percent of payroll for PERS employers and 12.56 percent for TRS employers and required the state fund the difference between the employer contribution and the full liability. This state obligation, often referred to as the state assistance or "on-behalf" payment, is calculated each year by the state's actuaries based on PERS/TRS asset valuations and forecasted liabilities. Between fiscal years 2006 and 2022, the state will have paid more than $8 billion in state assistance payments to the PERS and TRS systems, including a one-time lump sum deposit of $3 billion appropriated for fiscal year 2015.

The uniform cap on payroll contributions below the actuarial rate provides budget certainty for PERS and TRS employers; however, the 22 percent cap on state employee payroll limits the state's ability to incorporate the full cost within programs that are cost-shared by the federal government or funded by non-UGF sources. This under collection from non-UGF sources amounts to approximately $43 million annually.

How do we fix it?

Raising the employer contribution to the actuarial rate for all PERS and TRS participating employers would place a financial burden on plan participants. Rather than apply this change to all participants this legislation proposes lifting the cap for the State of Alaska only. By limiting the change only to the State of Alaska the stable rate is retained for other PERS and TRS employers. The legislation will increase the percentage of payroll for the State of Alaska from a fixed 22 percent to an annually actuarially determined rate, calculated at 30.11 percent in fiscal year 2022.

This change will be seen in the state budget as a reduction in the amount of the state assistance payment of close to $94 million UGF accompanied by an increase to payroll costs in state agencies by the same amount spread across multiple funding sources.

While this may seem like a net zero change, the shift allows the state to spread the cost among all fund sources instead of the unrestricted general funds used to make the state assistance payment. State employee payroll is charged across various fund sources depending on program cost allocation plans and an estimated $43 million will be shifted to federal and other non-UGF fund sources.

The table below shows estimates for the cost increases by fund group for each department as well as the associated reduction in the state assistance payment, which is normally shown under “statewide items” in the OMB and Legislative Finance fiscal summaries. The net reduction in unrestricted general fund spending is roughly $43 million in fiscal year 2022. These savings are projected to increase slightly each year with inflation and changes in the actuarial projections.

As this change is implemented in the budget, it is likely that some adjustments will be made on a case-by-case basis depending on the viability of various fund sources to absorb the increase. The intention is not to distribute “hollow” authority to agencies, but to capture additional funding where available and accurately reflect the cost of state employee payroll. The Office of Management and Budget will work with agencies to ensure that this cost shift is made appropriately.

FY22 Estimated Budget Impact	**UGF**	**DGF**	**Other**	**Fed**	**Total**
Agency Payroll Increase	51,713.5	4,585.2	24,920.7	13,780.6	0.0
State Assistance Payment Reduction	(95,000.0)	0.0	0.0	0.0	0.0
Total Budget Impact	**(43,286.5)**	**4,585.2**	**24,920.7**	**13,780.6**	**0.0**

Note: Alaska Marine Highway System payroll is not included in these estimates