



Representative Mike Kelly

House District 7 – Fairbanks

COMMITTEE TESTIMONY: House State Affairs Committee

Tuesday, March 22, 2005

As you know Alaska has a \$5 billion-plus unfunded liability in its public service pension programs. The future payout value of that liability is over \$15 billion. We are not alone. The problem is nationwide to one degree or another. One need only follow the adventures of Arnold in California to realize we are not alone – and our situation is not as dire as others. However, anyone who tells you we don't have a problem, or that it will just go away, or that Alaskans will allow us to write a check out of the Permanent Fund earnings reserve, is not your friend.

How did this dilemma happen when prior to 2000 our funds were typically nearly 100% funded and had remained so for decades? If you read the non-fiction Perfect Storm¹, or you lived through the '64 Alaska earthquake, or remember the '67 flood in Fairbanks, you know that negative factors can combine to create 100-year events. Our defined benefit pension funds experienced a perfect storm when the investment markets went down with the World Trade Centers, health care costs (particularly for the retired age group) skyrocketed, pension plan actuarials were updated reflecting the fact that the baby boomers are upon us and they will live longer than expected, and as a result of cutbacks in government over the past decade, there are fewer new and younger public service folks coming in the door to support those retiring.

There are those who are looking to blame some bad guys so we can put the boots to them and move on. That would be nice, but I believe the posse has found no evidence of fraud or misfeasance. Here is the usual list of folks we are inclined to blame: 1) how about the public employees? Sorry, they did nothing wrong. Their pension program is the one we provided for them. Any so-called abuses have been approved by the Legislature 2) Next is the pension boards and the money managers – sorry, there were some bad calls, but their errors in judgment are being pointed out by post-game armchair quarterbacks and these folks worked under close scrutiny, professional reporting requirements, and audits; 3) Next is the legislature, who are blamed for being too generous with public employee voters. Perhaps some blame may be justified here. But, except for approving a generous defined benefit program just like every other state used to have in place, the benefits we've passed out didn't cause a tenth of the problem; 4) Finally, the employers – they didn't pay enough into the fund – sorry, they historically paid in what the PERS/TRS boards required for 100% funding. They increased contributions fairly dramatically in years when it was required and they were permitted to reduce payments when full funding was reported. Maybe if you worked long and hard you could scare up 20% to blame on someone or another.

¹ *Junger, Sebastian. The Perfect Storm: A True Story of Men Against The Sea. 1998.*

But we'd still be stuck with a huge and growing problem. So what should we do? I know one thing we should not do, and that is wait until an election year to solve the problem. I sense there is little will among some legislators to act now. There will be next to no desire to take the steps required to fix the problem if we wait.

There are three bills before you today and the Senate is working on their solution. I believe the package before you would provide a workable solution. Yesterday I heard a legislator opine to a union leader that we might best write a check from the permanent fund earnings to extinguish the unfunded liability. I don't believe that non-beneficiary Alaskans would support that action. Others say just let the employers pay, even if it is as much as 25 to 40% or more of wages for the next 25 years. How can they possibly sustain that impact on labor costs? They would have to resort to large increases in property or sales taxes and I believe non-beneficiary voters would rebel.

Some say we should just reduce the liability to less than 100%. I question the wisdom of this approach. The Alaska pension system has maintained a 100% funding goal for retirement and retiree medical benefits. Recent fed rulings have confirmed that such a conservative approach is favored. Our problem is simple – we can no longer afford a defined benefit plan where the government absorbs all the risk associated with the retirement and retirement health care of our employees and teachers.

Lastly before we give a quick overview of the bills, I would like to point out that attracting and retaining high quality public employees and teachers must be a goal underlying any pension fix. If we fail at that, we risk our future. I agree with those who point out that public pay in Alaska has slipped and that generous benefits help us remain competitive. I have 11 grandchildren, 6 in public schools and 4 in private schools. I am related to many teachers and public employees in the Alaska system. I believe the bills before you today could help to unify a larger number of Alaskans behind a solution than would ignoring the problem and hoping it goes away, or writing a check out of permanent fund earnings, or raising local taxes dramatically.

Chairman Seaton tells me he intends to introduce a committee bill that will incorporate elements of my bills with other ideas from this committee. I support that approach, but encourage him to hurry. We have 40-some days left and the clock is running. I would like to see a bill sent to finance within a week after Easter break.

Here are the elements of our 3 bills:

- ✓ Board Fix
- ✓ Bring active un-retired employees to the table
- ✓ Put in place a defined contribution plan – Mercer alternative 2