GRS

Gabriel Roeder Smith & Company
Consultants & Actuaries

One Towne Square
Suite 800
Southfield, MI 48076-3723

248.799.9000 phone
248.799.9020 fax
www.gabrielroeder.com

March 15, 2017

Mr. George Hopkins
Executive Director
Arkansas Teacher Retirement System
1400 West Third Street
Little Rock, Arkansas 72201

Re: Senate Bill 218

Dear Mr. Hopkins:

You have asked for our analysis of Senate Bill (SB) 218 as it relates to the Arkansas Teacher Retirement System (ATRS). SB 218 modifies Arkansas Code Section 24-7-401 (c)(5)(B) concerning the employer's contribution to the ATRS. Our analysis reflects an amendment that we received on March 13, 2017.

Under the current statute the Board may increase the employer contribution rate above the 14% level beginning July 1, 2015 and each fiscal year thereafter, in increments of one fourth of one percent (0.25%) to a maximum of 15% of payroll only if the annual report from the System's actuary for the prior fiscal year indicates that the amortization period exceeds thirty (30) years without an increase in the employer rate. Section 24-7-401(c)(5)(B)(ii) provides that if a report by the System's actuary shows that the amortization period would be 30 years or less with an employer rate of 14%, then the employer rate shall not exceed 14%. Section 24-7-401(c)(5)(B)(iv) provides that if a report by the System's actuary shows that the System's amortization period would be 30 years or less with an employer contribution rate below the current level, then the employer contribution rate shall be the greater of 14% or the rate required to amortize unfunded liabilities over 30 years. Effectively, the statute states that if the employer rate is raised above the 14% level, it must be reduced if it becomes possible to amortize the unfunded liabilities over 30 years with a lesser employer rate. However, the reduced rate is not allowed to fall below 14% even if the unfunded liabilities can be amortized over less than 30 years. Under current statutes, then, 30 amortization years is a key threshold in determining adjustments to the employer contribution rate.

Senate Bill 218 modifies §§24-7-401(c)(5)(B)(i) and (ii) by replacing the 30 year threshold with an 18 year threshold for the process of adjusting the employer rate. Specifically, §24-7-401(c)(5)(B)(i) allows the Board to increase the employer contribution rate above 14% beginning July 1, 2018 and for fiscal years thereafter in increments of one-fourth of one percent (0.25%) per fiscal year if the System's amortization period is greater than 18 years. The maximum total increase permitted under the bill is to 15% of payroll. Senate Bill 218 also modifies Section 24-7-401(c)(5)(B)(ii) to provide that if the System's amortization period would be 18 years or less with an employer rate of 14% of payroll, then the employer rate shall not exceed 14% of payroll. Finally Senate Bill 218 repeals current §24-7-401(c)(B)(iv) which required a minimum employer contribution rate of 14% even if the amortization period to pay unfunded liabilities is less than 30 years.

Actuarial practice is moving in the direction of amortization periods shorter than 30 years. Senate Bill 218 brings ATRS more in line with emerging actuarial practice by removing certain statutory references to 30 years, and instead targeting a period of 18 years. Senate Bill 218 is financially favorable for ATRS because it allows for an increase in employer contributions if the amortization period is greater than 18 years rather than 30 years. Consequently, SB 218 will help ATRS meet its funding objectives sooner than otherwise would be the case. SB 218 does remove a requirement to keep the employer contribution rate at 14% even if the amount required to amortize the unfunded accrued liability is less than or equal to 30 years.

Senate Bill 218 does not require an increase in the employer contribution rate, but rather permits an increase, if the amortization period exceeds 18 years. An increase in the employer contribution rate from its present level of 14% of payroll to 14.25% of payroll would reduce the amortization period from the present level of 29 years to just below 28 years.

Users of this information should be aware that estimates of changes in amortization period are heavily dependent on actuarial assumptions and on the amortization period before the change. Please refer to the full actuarial report of the June 30, 2016 valuation for a complete description of actuarial assumptions and methods.

We hope this analysis meets your needs.

Please review this letter carefully to ensure that we have understood the bill properly. The analysis in this letter should not be relied upon if there is doubt about our understanding of the bill. Our analysis relates only to the plan changes described in this correspondence. In the event that other plan changes are being considered, it is very important to remember that the results of separate actuarial analyses cannot generally be added together to produce a total. The total can be considerably greater than the sum of the parts due to the interaction of various plan provisions with each other, and with the assumptions that must be used.

We did not review this bill for compliance with Federal, State, or local laws or regulations, and internal revenue code provisions nor did we attempt to determine whether these changes would contradict or negate other related State, or local laws or legislation currently under consideration. Such a review was not within the scope of our assignment.

Brian B. Murphy, Judith A. Kermans and Heidi G. Barry are Members of the American Academy of Actuaries (MAAA) and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

This communication shall not be construed to provide tax advice, legal advice or investment advice.

Sincerely,

Judith A. Kermans

Judith A. Kermans, EA, MAAA, FCA

Brian B. Murphy

Brian B. Murphy, FSA, EA, MAAA, FCA

Heidi G. Barry

Heidi G. Barry, ASA, MAAA