

March 1, 2013

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

**Re: Senate Bill 160**

Dear Mr. Hopkins:

You have asked us for our analysis of Senate Bill 160 as it relates to the Arkansas Teacher Retirement System (ATRS).

**Section 1 of SB 160** amends Arkansas Code Section 24-7-202(27) concerning the definition of salary. The specific changes are:

- a. Subsection (27)(A) is modified to provide that generally, remuneration that is subject to federal income tax withholding is to be considered salary whether or not the employer actually withholds tax from the remuneration.
- b. Subsection (27)(B) is modified to continue to permit incentive bonuses paid to an employee in connection with certification by the national Board for Professional Teaching Standards to continue to count as salary, but only if the Department of Education pays the employer contribution and the member pays the required member contribution.
- c. Subsection (27)(C) is introduced that excludes the following from salary:
  - Payments made as a result of a contract buyout agreement, settlement, etc. on which the employer is required to withhold federal income tax unless the amount paid to the member is higher than the member's regular service wage. Our understanding is that in cases where the payments are counted as salary, the payments will not be stacked on top of existing wages, but rather that existing wages will then not be counted as salary.
  - All non-monetary taxable income such as vehicles, housing, etc.
- d. Subsection (27)(D) is introduced that permits the ATRS Board to promulgate rules to modify the definition of salary.

**Section 2 of SB 160** amends Section 24-7-735 concerning the calculation of benefits in connection with contract buyout agreements as follows.

- a. Section 24-7-735(a) is expanded to include settlements, judgments, arbitration awards, and decrees in addition to buyouts.
- b. Section 24-7-735(b) is modified to provide that employer contributions are only payable on payments for which the employer is required to withhold federal income tax.
- c. Section 24-7-735(c) is introduced to require the employer to provide certain legal documentation to ATRS and to provide that a member cannot receive salary credit or service credit under a settlement agreement or court order unless permitted by Section 24-7-735.
- d. Section 24-7-735(d) is introduced allowing the purchase of service credit under a settlement agreement or court order for a wrongful termination with certain stipulations. The service credit is to be purchased on an actuarially equivalent basis

**Section 3 of SB 160** repeals Section 24-7-737 related to additional remuneration. Section 24-7-737 provided great latitude to members regarding various types of additional remuneration as earnings for purposes of retirement benefits. The section required the payment of employer and employee contributions on the remuneration in order to establish it as salary. Section 24-7-737 also permitted other than cash remuneration to be counted as salary.

Our understanding, based on discussions with ATRS staff it that the intent of SB 160 is to narrow the definition of salary to wages earned. The bill would prohibit nonmonetary compensation from being treated as salary, clarify the status of contract buyout payments, and allow the purchase of time related to wrongful termination at actuarial equivalent rates. Allowing a terminated employee or the employer to purchase service related to wrongful termination settlements on an actuarially equivalent basis could lead to a reduced need for difficult damage calculations in court. Also, it is likely to reduce confusion and misunderstanding related to large payments by employers in connection with litigation. Finally the bill grants authority to the ATRS Board to set certain parameters for salaries to be used in the calculation of member benefits.

This bill is primarily administrative in nature. We think it is likely to generate a small savings by narrowing the definition of salary and therefore reducing the number of cases where a person's ATRS benefit can be significantly increased due to a settlement or other unusual remuneration. The savings is likely to be too small to affect the funding status of ATRS or the amortization period.

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 law or regulations, or internal revenue code provisions. Such a review was not within the scope of our assignment.

Mr. George Hopkins

March 1, 2013

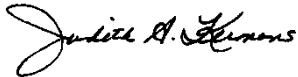
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The undersigned are Members of the American Academy of Actuaries and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinion contained herein.

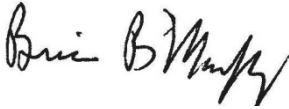
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Sincerely,



Judith A. Kermans, EA, MAAA, FCA



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

JAK/BBM:sc