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March 28, 2013

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

Re: HB 1198 as engrossed 3/26/2013

Dear Mr. Hopkins:

You have asked us for our analysis of House Bill (HB) 1198 (as engrossed) as it relates to the Arkansas Teacher Retirement System (ATRS).

HB 1198 creates Subchapter 17 of title 24, Chapter 7 of the Arkansas Code authorizing the Board of Trustees to create a Tier II benefit plan within the Arkansas Teacher Retirement System. The Tier II plan, if created, would apply to all members initially hired on or after July 1, 2015, and only to such members. The Tier II plan must provide the same benefits that are currently provided by the Arkansas Teacher Retirement System except that a Tier II plan may modify the cost-of-living adjustment (COLA) by resolution at a meeting of the board. The Tier II COLA must be a “simple” adjustment. It must not exceed 3%. It may be tied to an inflation index and is limited to future fiscal years.

When a Tier II plan is introduced, plan costs *do not* change all at once. Rather, costs would change gradually over time as an increasing number of new members are covered by the Tier II plan. We understand that the Board’s intent in this situation would be to maintain the present COLA for all members, including those members who would eventually be in a Tier II plan. Therefore, we expect no immediate savings from this bill since no actual changes in benefits are currently anticipated.

However, HB 1198 provides the Board with important added flexibility in dealing with potential future funding issues. In order to understand the financial impact that this flexibility might have, we modeled the introduction of a Tier II plan with a COLA that is 1% lower (i.e. 2% instead of 3%) than the COLA currently in effect. Such a plan would provide a savings that would affect the amortization period in approximately the same manner as 0.36% change in the employer contribution rate. The amount actually saved over time will depend on the specifics of the Tier II plan.

We hope this analysis meets your needs.

Please review this letter carefully to ensure that we have understood the bill properly and that the assumptions we have made are realistic. The analysis in this letter should not be relied upon if there is doubt about our understanding of the bill or the assumptions we have made. 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. Such a review was not within the scope of our assignment.

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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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

JAK/BBM:rmn