1. **Why have the TRS and ERS funding levels dropped?**

   Answer: Funding levels for all systems across the country including TRS and ERS have dropped over the last 11 years. While there are a number of reasons that these levels have dropped, each system may have experienced more or less of an effect depending on their specific situation:

   A. COLAs granted to retirees
   B. Modification of amortization periods
   C. Investment returns in the short term less than the expected long-term rate

2. **Why have they fallen below the national average funding levels?**

   Answer: More specifically, the TRS and ERS funding ratios have changed as a result of several factors:

   A. COLAs granted to retirees—For example, the Legislature granted COLAs of 4% effective 10/1/2000, 3% effective 10/1/2002, 4% effective 10/1/2005, and 7% effective 10/1/2006.To illustrate the effect of COLAs, the funded ratio changed from 93.6% to 89.6% from 9/30/2003 to 9/30/2004 (reflecting the COLA effective 10/1/2005) and then to 83.6% as of 9/30/2005 (reflecting the COLA effective 10/1/2006). While there are many factors that are included in the actuarial valuations, for 2004 and 2005, a large contributing factor reducing the funded ratio was the COLAs.

B. In 2010 the legislature changed the amortization period from 20 years to a period not to exceed 30 years. This factor contributed to a reduction in the funded ratio. By extending the amortization period, employer contributions to the plan were lowered; thereby, lowering the funded percentage when compared to where it would be had the 20-year amortization period been maintained.

C. While current RSA returns have not been at the long-term projected rate per the actuarial assumptions, the returns have been above appropriate benchmarks for the last 10 years as illustrated by the table below:

Type Benchmark	Benchmark	Benchmark Rate	TRS	ERS
Domestic Equities	Russell 3000	3.48%	3.72%	3.74%
Bond Market Index	Barclay's Aggregate	5.66%	6.56%	6.49%
Net Int'l Equity	MISC EAFE	5.03%	5.74%	5.75%

Further, when comparing RSA returns to other pension plans, most others are calculated as of June 30 rather than September 30. When the equity markets fall significantly in the quarter ended 9/30 (as they did last year), the TRS and ERS market value is lower at the valuation date (Sept. 30) as compared to other funds valued as of June 30. Therefore, the TRS and ERS funded ratios when compared to others tend to be slightly lower.

3. **I've always been told that Alabama's government tends to pay more to support the pension funds when these funding levels decline and to pay less when they rise. Is that accurate? If so, is that a reason why these funding levels are important?**

   Answer: The lower the funded ratio, the higher the employer contribution rate in order to fund the plan at the actuarially determined Annual Required Contribution rate (ARC).

4. **What is the outlook for future funding levels?**

   Answer: Funding levels will likely continue to drop over the next few years, but ultimately depend on the market returns in the future.

5. **What, if anything, can be done by the state or the TRS/ERS boards to slow and reverse the decline in funding levels? What do you think should be done?**

   Answer: The state Legislature together with the RSA has already put into place several important changes that over time will affect the funded ratio:

   A. Repealed the DROP program effective March 24, 2011
   B. Increased employee contributions effective October 1, 2011
   C. Created a Tier 2 benefit plan for new hires effective on or after January 1, 2013

6. **Is the steady decline in funding levels a concern for you, and is it a concern for the state? Why or why not?**

   Answer: Many people tend to think that funding level is the most important indicator of whether or not a pension plan is healthy. While it is certainly one component, the most important indicator is whether or not the ARC or Annual Required Contribution is being made to the fund. For TRS and ERS, the state has always contributed the ARC. This has been something that RSA has fought hard to maintain due to its importance to the plan. If a plan has a higher funded ratio than ours but does not receive the Annual Required Contribution, the health of that fund would be significantly less than the health of the ERS or TRS.

   Finally, RSA worked together with the Governor's Office and the Legislature in the 2012 legislative session to design a Tier 2 plan for new hires. This Tier 2 new hire plan is significant in that over the years, less money will be required to fund pension costs for the Tier 2 plan; and therefore, more resources will be available to fund the existing unfunded liability. This is not an overnight fix—we must be patient as this ship is slowly turned.