Select Committee on Pension Policy

P.O. Box 40914
Olympia, WA 98504-0914
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Regular Committee Meeting

November 18, 2008
10:00 a.m. – 12:00 p.m.
Senate Hearing Room 4
Olympia

AGENDA

10:00 a.m.	**(1)**	**Approval of Minutes**
10:05 a.m.	**(2)**	**Assistant Attorney General Report – Mary Ellen Combo, Senior Assistant Attorney General**

Work Session

10:20 a.m.	**(3)**	**Visiting International Faculty – Laura Harper, Policy and Research Services Manager**
10:35 a.m.	**(4)**	**Change Membership Default for Plans 2/3 – Dave Nelsen, Senior Policy Analyst**
10:55 a.m.	**(5)**	**Interruptive Military Service Credit – Laura Harper**
11:05 a.m.	**(6)**	**Plan 1 COLA Proposals – Darren Painter, Policy Analyst**

Public Hearing with Possible Executive Session

11:20 a.m.	**(7)**	**DRS Technical Corrections – Laura Harper**
11:30 a.m.	**(8)**	**OSA Request Legislation – Laura Harper**
11:40 a.m.	**(9)**	**SERS Past Part-time Service Credit – Darren Painter**
11:50 a.m.	**(10)**	**$150,000 Death Benefit – Darren Painter**
Noon	**(11)**	**Adjourn**

**These times are estimates and subject to change depending on the needs of the Committee.*

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Select Committee on Pension Policy

2008 Meeting Dates

January 15, 2008 . *canceled*
February 12, 2008 . *canceled*
March 18, 2008 . *canceled*
April 15, 2008
May 13, 2008
June 17, 2008
July 15, 2008
August 12, 2008 . *canceled*
September 16, 2008
October 21, 2008
November 18, 2008
December 16, 2008

JANUARY

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Reserved Subgroup Dates

SHR4
2:00 - 4:00pm - Mondays
January . *none scheduled*
February . *none scheduled*
March . *none scheduled*
April 14, 2008 . *none scheduled*
May 12, 2008 . *none scheduled*
June 16, 2008 . *none scheduled*
July 14, 2008 . *none scheduled*
August 11, 2008 . *canceled*
September 15, 2008 . *none scheduled*
October 20, 2008 . *none scheduled*
November 17, 2008 . none scheduled
December 15, 2008

Goals for Washington State Public Pensions

Revised and Adopted September 27, 2005

1. Contribution Rate Setting: To establish and maintain adequate, predictable and stable contribution rates, with equal cost-sharing by employers and employees in the Plans 2, so as to assure the long-term financial soundness of the retirement systems.

2. Balanced Long-Term Management: To manage the state retirement systems in such a way as to create stability, competitiveness, and adaptability in Washington's public pension plans, with responsiveness to human resource policies for recruiting and retaining a quality public workforce.

3. Retirement Eligibility: To establish a normal retirement age for members currently in the Plans 2/3 of PERS, SERS, and TRS that balances employer and employee needs, affordability, flexibility, and the value of the retirement benefit over time.

4. Purchasing Power: To increase and maintain the purchasing power of retiree benefits in the Plans 1 of PERS and TRS, to the extent feasible, while providing long-term benefit security to retirees.

5. Consistency with the Statutory Goals within the Actuarial Funding Chapter: To be consistent with the goals outlined in the RCW 41.45.010:

    a. to provide a dependable and systematic process for funding the benefits to members and retirees of the Washington State Retirement Systems;
    b. to continue to fully fund the retirement system plans 2 and 3, and the Washington State Patrol Retirement System, as provided by law;
    c. to fully amortize the total costs of PERS 1, TRS 1 and LEOFF 1, not later than June 30, 2024;
    d. to establish predictable long-term employer contribution rates which will remain a relatively predictable portion of future state budgets; and
    e. to fund, to the extent feasible, benefit increases over the working lives of those members so that the cost of those benefits are paid by the taxpayers who receive the benefit of those members' service.

2007 Rules of Procedure

RULE 1. Membership. The Committee shall consist of 20 members: two from each caucus of the legislature, four active members or representatives of active members of the state retirement systems, two retired members or representatives of retired members of the state retirement systems, four employer representatives, and the Directors of the Department of Retirement Systems and the Office of Financial Management.

The Directors of the Department of Retirement Systems and the Office of Financial Management may appoint alternates from their respective agencies for membership on the SCPP.

RULE 2. Meetings. The Select Committee on Pension Policy (SCPP) will typically meet once each month during the Legislative Interim. Meetings may be called or cancelled by the Chair of the SCPP or Executive Committee as deemed necessary.

RULE 3. Rules of Order. All meetings of the SCPP, its Executive Committee, or any subcommittee created by the SCPP shall be governed by Reed's Parliamentary Rules, except as specified by applicable law or these Rules of Procedure.

RULE 4. Quorum. A majority of the 20 committee members shall constitute a quorum of the Full Committee (11 members). A majority of the members appointed to a subcommittee shall constitute a quorum of the subcommittee.

RULE 5. Voting. A majority of the 20 committee members must vote in the affirmative for an official action of the SCPP to be valid (11 members); a majority of those committee members present must vote in the affirmative on procedural matters (at least six members), unless provided otherwise in statute or these Rules of Procedure. Examples of official actions of the SCPP include: recommendations, endorsements, statements, or requests made by the SCPP to the Legislature, the Pension Funding Council, or any other body; election of officers; approval of minutes; adopting rules of procedure; and adopting goals. Examples of procedural matters include: convening or adjourning meetings; referring issues to the Executive Committee or subcommittees; and providing direction to staff. A majority of the members appointed to a subcommittee must vote in the affirmative for an official action of a subcommittee to be valid; a majority of those subcommittee members present must vote in the affirmative on procedural matters, unless provided otherwise in statute or these Rules of Procedure.

RULE 6. Minutes. Minutes summarizing the proceedings of each SCPP meeting and subcommittee shall be kept. These minutes will include member attendance, official actions taken at each meeting, and persons testifying.

RULE 7. SCPP Chair, Vice Chair, Executive Committee and Subcommittees. An Executive Committee shall be established and shall include six members. Reorganization elections shall take place at the first meeting of the year as follows: First the Chair shall be elected and then the Vice Chair shall be elected. The Chair shall be a member of the Senate in even-numbered years and a member of the House of Representatives in odd-numbered years. The Vice Chair shall be a member of the House in even-numbered years and a member of the Senate in odd-numbered years.
Three members of the Executive Committee shall then be elected, one member representing active members, one member representing employers, and one member representing retirees. In addition, the Director of the Department of Retirement Systems shall serve on the Executive Committee.

Executive Committee members may designate an alternate to attend Executive Committee meetings in the event they cannot attend. Designations shall be made in the following manner:

a. The Chair and Vice Chair shall designate an SCPP member who is a legislator from the same house.
b. The Director of the Department of Retirement Systems shall designate an employee of the department.
c. Active, Employer, and Retiree member representatives shall designate an SCPP member representing their member group.

Subcommittees of the SCPP may be formed upon recommendation of the Executive Committee. The creation of the subcommittee and appointment of members shall be voted on by the full SCPP.

RULE 8. Duties of Officers.

A. The Chair shall preside at all meetings of the SCPP and Executive Committee, except that the Vice Chair shall preside when the Chair is not present. In their absence, an Executive Committee member may preside.

B. The State Actuary shall prepare and maintain a record of the proceedings of all meetings of the SCPP Committee, Executive Committee, and SCPP Subcommittees.

C. The Executive Committee shall perform all duties assigned to it by these Rules of Procedure, such other duties delegated to it by the SCPP, and shall set meeting agendas and recommend actions to be taken by the SCPP.

D. A recommendation to refer an issue to the Assistant Attorney General will be approved by the Chair or by a majority vote of the Executive Committee. The Chair or the Committee will consider priorities of the SCPP of all legal issues and budget constraints in making this decision.

Advice from the Attorney General's Office to the Chair or the Committee may be subject to the attorney client privilege. When subject to the privilege, Committee members are advised to maintain the advice as confidential. The privilege may be waived only by vote of the Committee.

E. The State Actuary may refer requests for information or services by Select Committee on Pension Policy members that are directly related to current Committee projects or proposals and/or require a significant use of OSA resources to either the Chair of the SCPP or the Executive Committee. Such requests will be approved by either the Chair or by a majority vote of the Executive Committee prior to initiation and completion by the OSA. The Executive Committee will consider priorities of all current OSA projects and budget constraints in making this decision.

F. The State Actuary shall submit the following to the Executive Committee and the full SCPP for approval: the biennial budget submission for the OSA, and any personal services contract of $20,000 or more that is not described in the biennial budget submission.

G. The Chair and Vice Chair shall appoint four members of the SCPP to serve on the State Actuary Appointment Committee. At least one member shall represent state retirement systems' active or retired members, and one member shall represent state retirement system employers. The Chair and Vice Chair may designate an alternate for each appointee from the same category of membership.

RULE 9. Expenses. Legislators' travel expenses shall be paid by the member's legislative body; state employees' expenses shall be paid by their employing agency; other SCPP members' travel expenses shall be reimbursed by the Office of the State Actuary in accordance with RCW 43.03.050 and 43.03.060.

RULE 10. Staff. The OSA shall provide staff and technical assistance to the Committee. The State Actuary has the statutory authority to select and employ such research, technical, clerical personnel, and consultants as the State Actuary deems necessary. The State Actuary shall inform the Executive Committee of final personnel actions. Any employee terminated by the State Actuary shall have the right of appeal to the Executive Committee. The State Actuary has also implemented a grievance procedure within the OSA. Any employee who has followed the OSA grievance process and disagrees with the outcome may appeal to the Executive Committee. Employee appeals must be filed in writing with the Chair within 30 days of the action being appealed.

Effective Date June 19, 2007.

Revised June 19, 2007 by the Select Committee on Pension Policy.

Chair - Representative

Vice Chair - Senator

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1. Approval of Minutes

Select Committee on Pension Policy

P.O. Box 40914
Olympia, WA 98504-0914
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REGULAR COMMITTEE MEETING
October 21, 2008
DRAFT MINUTES

The Select Committee on Pension Policy met in Senate Hearing Room 4, Olympia, Washington on October 21, 2008.

Committee members attending:

Senator Schoesler, Chair	Senator Hobbs
Representative Conway, Vice-chair	Senator Holmquist
Representative Bailey	Bob Keller
Don Carlson	Sandra Matheson
Lois Clement	Doug Miller
Representative Crouse	Victor Moore
Charles Cuzzetto	Glen Olson
Randy Davis	J. Pat Thompson
Representative Fromhold	David Westberg

Senator Schoesler, Chair, called the meeting to order at 10:09 a.m.

(1) APPROVAL OF MINUTES

Moved, seconded, and carried to: Approve the Regular Committee Meeting September 16, 2008, Draft Minutes.

(2) STATE INVESTMENT BOARD, UPDATE

Joe Dear, Executive Director, Washington State Investment Board (WSIB), gave an update on market developments and WSIB performance.

No action taken.

(3) SEPTEMBER 2008 ECONOMIC AND REVENUE FORECAST COUNCIL

Arun Raha, Executive Director, Washington State Economic and Revenue Forecast Council, reported on the "State Economic Outlook."

No action taken.

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(4) DISABILITY BENEFITS

Dave Nelsen, Senior Policy Analyst, reported on "Disability Benefits."

No action taken.

(5) SERS PAST PART-TIME SERVICE CREDIT

Darren Painter, Policy Analyst, reported on "SERS Past Part-Time Service Credit."

No action taken.

(6) OSA REQUEST LEGISLATION

Laura Harper, Policy and Research Services Manager, reported on "OSA Request Legislation."

No action taken.

(7) $150,000 DEATH BENEFIT

Darren Painter reported on "$150,000 Death Benefit."

No action taken.

(8) FISH AND WILDLIFE SERVICE CREDIT TRANSFER

Dave Nelsen reported on "Fish and Wildlife Service Credit Transfer."

No action taken.

Public testimony gvien by:

Matt Zuvich, Washington Federation of State Employees

Bruce Bjork, Washington Department of Fish and Wildlife

(9) 2009 SCPP MEETING DATES

Kelly Burkhart, Administrative Services Manager, reported on the "2009 SCPP Meeting Dates."

Moved, seconded, and carried to: Adopt the 2009 SCPP meeting dates at the December 16, 2008 meeting.

The meeting adjourned at 12:30 p.m.

Recorded audio of Select Committee on Pension Policy meetings is often available free of charge at www.tvw.org. Additionally, you may request a CD-ROM copy of the audio. Please contact the Office of the State Actuary for further information.

2. Assistant Attorney General Report

USE OF PUBLIC RESOURCES AND BALLOT MEASURES

The State Ethics Law, chapter 42.52 RCW, governs the actions of state officers and employees.

RCW 42.52.180 governs the use of public resources for political campaigns.

> No state officer or state employee may use or authorize the use of facilities of an agency, directly or indirectly, for the purpose of assisting a campaign for election of a person to an office or for the promotion of or opposition to a ballot proposition.
>
> Facilities of an agency include, but are not limited to, use of stationery, postage, machines, and equipment, use of state employees of the agency during working hours, vehicles, office space, publications of the agency, and clientele lists of persons served by the agency.

There are exceptions to the prohibition on using state resources to support the election of a candidate or to oppose or support a ballot proposition:

1. Conducting research into the impact of a ballot proposition, only gathering the facts directly related to the agency's responsibilities. The research cannot be skewed to support or oppose the ballot proposition, but must be neutral.
2. Publishing factual information showing the comparative effects of the ballot proposition. Again, the factual information must be neutral.
3. Responding to public records requests from supporters or opponents of the ballot proposition. All must be treated alike as to the manner of response, the timing and any exemptions claimed.
4. For elected officials, one may make statements supporting or opposing a ballot proposition at an open press conference, or in response to a specific inquiry, but there may not be any actual and measurable expenditure of public funds.
5. Elected officials may use public facilities to communicate their views on ballot propositions that may affect a matter that falls within their responsibilities.
6. An elected legislative body may collectively endorse or oppose a ballot measure if the required meeting notice contains the title and number of the ballot proposition and equal opportunity is allowed for expression of opposing viewpoints.

The SCPP is not an elected legislative body. Some legislators, who are elected officials, serve on the SCPP; however, they are part of the SCPP when attending SCPP meetings, and the exceptions listed above do not apply to them when they are acting as part of the SCPP.

ATTORNEY-CLIENT PRIVILEGE

The SCPP has not had its own Assistant Attorney General (AAG) before so it is important that each member understand how the attorney-client relationship works.

Per the SCPP Procedural Rules, Rule 8.D, only the Executive Committee or the Chair of the Committee may request legal advice from the assigned Assistant Attorney General. Rule 8.D: "A recommendation to refer an issue to the Assistant Attorney General will be approved by the Chair or by a majority vote of the Executive Committee."

Legal advice is provided to either the Executive Committee or the Chair. The Executive Committee will determine how to transmit legal advice to the full Committee.

Any communication between an attorney and his or her client is privileged, which means that the communication is confidential and cannot be disclosed to anyone who is not a client or a member of that client group. This privilege is contained in statute (RCW 5.60.060(2)(a)) and in the Rules of Professional Conduct that apply to attorneys (RPC 1.6). The privilege fosters open communication between the attorney and the client.

The attorney-client communication may be verbal or in writing. Only substantive communications between the attorney and the client are protected by the privilege. A communication to set up meetings, for example, is not a privileged communication.

For an attorney who represents a governmental agency, the duty of confidentiality is owed to the governmental agency, not to individual employees of the organization.

The privilege belongs to the client and only the client can waive the privilege. The SCPP is the client but by its own procedural rules it has determined that only the Executive Committee may waive the privilege.

Rule 8.D of the SCPP procedural rules states: "The privilege may be waived only by vote of the Committee."

No individual member of the Committee can choose to ignore the privilege and disclose privileged information without the express authorization of the Executive Committee. Disclosure without authorization of the Executive Committee may result in allegations that the privilege has been waived. Rule 8.D of the SCPP Procedural Rules states: "When subject to the privilege, Committee members are advised to maintain the advice as confidential."

If a member does reveal a privileged communication, the Executive Committee and the AAG should remind that member about the attorney-client privilege and that only the Executive Committee can waive the privilege.

Communications from me to the Executive Committee or the Chair will be marked in bold that the advice is protected by the attorney-client privilege. The usual notation will be:

ATTORNEY/CLIENT PRIVILEGED COMMUNICATION

DO NOT DISSEMINATE FURTHER WITHOUT THE APPROVAL OF THE SCPP EXECUTIVE COMMITTEE

Understand that when a written document from me is stamped attorney-client privilege this means the following:

> You should not share this memorandum with anyone outside the agency unless and until the Executive Committee decides to waive the privilege. To prevent an inadvertent waiver of this privilege, you should avoid referring to this memorandum or other confidential communication in public and/or during committee meetings, until and unless the privilege has been waived. You may discuss the subjects covered in the memorandum without specifically referring to this document or its author. For example, if the AAG provided written advice on the interpretation of a statute, it would be permissible to adopt that position on the statute's interpretation as your own and discuss it in a meeting. You cannot however attribute the comment as having come from the AAG or discuss receiving a legal memo as that would reveal the attorney-client communication.

3. Visiting International Faculty

Visiting International Faculty

Description of Issue

Should visiting teachers from other countries be exempt from retirement system membership?

The Visiting International Faculty Program (VIF) is a sponsor under the U.S. Department of State's Exchange Visitor Program. VIF would like to sponsor visiting teachers in Washington, and is requesting an exemption from membership in TRS Plan 2/3. These teachers would not stay in the state long enough to earn a pension. Exempting them would mean that employer and member contributions would not be collected for these teachers, and refunds of member contributions would not be required when they leave.

Based on experience in other states, the program could grow to about 200-300 teachers statewide.

Policy Highlights

- A similar exemption exists in TRS Plan 1.
- DRS supports the idea of the exemption to alleviate administrative concerns.
- The two peer states that participate in the Exchange Visitor Program provide an exemption.
- An exemption is consistent with federal policies.
- An exemption adds membership complexity.
- An exemption spreads Plan 1 UAAL cost to non-participating employers.
- Impacts would reach beyond the pension system.

Possible Strategies and Next Steps

The SCPP could sponsor or endorse legislation on this issue, request further study, monitor the issue in the future or take no action. The Executive Committee will consider possible strategies and decide whether to direct staff to provide a bill draft and draft fiscal note.

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Visiting International Faculty

In Brief

ISSUE

Should the SCPP recommend legislation to exempt visiting teachers from other countries from membership in the Teachers Retirement System Plans 2 and 3 (TRS 2/3)?

MEMBER IMPACT

The proposal would impact TRS 2/3 beginning in the 2010-2011 school year. If legislation were passed, the proponents intend to place approximately 20 visiting international teachers in Washington in the first year, depending on the economy. Based on experience in other states, the program could grow to about 200-300 teachers statewide.

According to the 2007 Actuarial Valuation Report there are approximately 58,600 active members in TRS 2/3.

Laura Harper
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Current Situation

The Director of Government Relations for the Visiting International Faculty Program (VIF) reports that several school districts have asked VIF to bring international teachers to Washington. Also, according to VIF, teachers around the world are expressing interest in working in Washington. Typically VIF seeks to address statutory and regulatory concerns prior to bringing teachers to a specific state. VIF requests a statutory change to the Teachers' Retirement System Plans 2 and 3 (TRS 2/3). The proposal would exempt visiting international teachers from retirement system membership.

Under current TRS 2/3 provisions, visiting teachers who come from other countries to work full time on a temporary basis are required to become contributing members of TRS Plan 2 or 3. When they leave employment they are eligible for a refund of their member contributions.

TRS History

TRS Plan 1 has the following membership exemption: "All teachers employed full-time in the public schools shall be members of the system *except alien teachers who have been granted a temporary permit to teach as exchange teachers.*" (Emphasis added.) TRS 1 closed in 1977. The membership exemption was not continued in TRS 2/3. The reason for discontinuing the exemption is unknown, but we do know that many ancillary benefits were discontinued or reduced when Washington closed Plan 1 and opened the Plans 2/3.

What is the VIF Program?

VIF was founded in 1989 and provides U.S. schools with full-time visiting teachers from fifty nations. Teachers serve for one to three years. The program provides screening, preparation, and support services for visiting teachers.

The VIF Program is a private organization and a designated sponsor in the Exchange Visitor Program under the U.S.

Department of State. The Exchange Visitor Program is carried out under a federal act entitled the Mutual Educational and Cultural Exchange Act of 1961. Its purpose is to foster mutual understanding between the people of the United States and the people of other countries through educational and cultural exchanges.

All exchange visitors are expected to return home upon completion of their program in order to share their U.S. experiences with people in their home country. As stated in federal regulations, these exchanges enable visitors to better understand American culture, society, and teaching practices at the primary and secondary levels. See 22 CFR 62.24(a). They also enhance American knowledge of foreign cultures, customs, and teaching approaches.

Federal regulations set minimum requirements for visitor eligibility. Sponsors such as the VIF Program must adequately screen teacher qualifications, reputation, and character prior to accepting them into the program. Visiting teachers must receive a special visa (known under the regulations as a "J-1" visa) and may participate in the program for a maximum of three years. They also must obtain a Social Security card and pay taxes on salary or wages earned in the U.S., although some are subject to bilateral tax treaties affecting federal taxation. FICA payments are triggered after 180 days, unless they already have a Social Security card from previous work or study in the U.S.

VIF is a sponsor under the U.S. Department of State's Exchange Visitor Program.

VIF is the largest U.S. sponsor for teachers in the State Department's Exchange Visitor Program. The State Department does not recommend or "rate" any of the designated sponsors, however; by virtue of its State Department status, the VIF Program has complied with all applicable regulations for obtaining designation and is in good standing.

There are approximately sixty other sponsors for teachers under the federal program; however, most of these place very few teachers compared to VIF. According the VIF's Director of Government Relations, the second largest sponsor in the U.S. is the Ministry of Education for the Spanish Embassy, which places no more than about 400 teachers per year nationwide. VIF partners with the Ministry in some states to recruit and support teachers from Spain.

Other States

Two peer states, California and Florida, participate in VIF's program. Their visiting teachers are exempt from retirement system membership.

The VIF Program reports that it currently sponsors about 1,500 teachers in 1,000 schools within seven participating states. Once VIF moves into a state, it allows the program to grow. On average, programs in other participating states have grown to about 200-300 visiting teachers per year.

Currently the VIF Program provides teachers in two of Washington's peer states: California and Florida. Both of these states exempt visiting teachers from retirement system membership. Florida requires a temporary visa and has a three-year limit on exempt employment. (These requirements are consistent with federal regulations.) California's membership exemption is much broader and simply excludes "exchange teachers or sojourn teachers from outside of this state" from retirement system membership.

The VIF Program started in North Carolina. In addition to California and Florida, VIF places teachers in Georgia, Maryland, South Carolina, and Virginia. At this time, all participating states have membership exemptions for participants except Maryland. (The VIF Program has not yet asked for an exemption there.)

Policy Analysis

The issue for policy makers is whether to exempt visiting teachers from other countries from membership in TRS 2/3. This section will summarize the impacts on TRS of providing the proposed exemption. It will also discuss the pros and cons of a membership exemption from a policy perspective. Finally, this section identifies questions that reach beyond the pension system, and which may be of interest to other legislative committees and/or groups.

How Would the Proposal Impact TRS?

Currently, visiting teachers from other countries who teach full-time in eligible positions must pay member contributions to the retirement system. Similarly, their employers must pay contributions on their behalf. When their visas expire and they leave their teaching positions, they can apply for

Visiting teachers stay for one to three years and do not earn a pension.

refunds of member contributions. The employer contributions remain with TRS.

Under the proposal, temporary visiting teachers would be exempt from retirement system membership. This means that the Department of Retirement Systems (DRS) would not collect member or employer contributions for these teachers. No service credit would accrue and DRS would have no obligation to provide refunds of member contributions after visiting teachers leave employment.

How many positions would be affected in TRS? Passing the exemption would trigger action by VIF to work with school districts to temporarily fill certain TRS positions with visiting teachers. The proponents have stated that they intend to place approximately twenty visiting teachers in the 2010-2011 school year, depending on the economy.

Within a four- to five-year period VIF would allow the program to grow. Looking at programs in other states, full program capacity would mean a presence of 200-300 temporary visiting teachers within the state. (Note: While there are other designated sponsors under the State Department's Exchange Visitor Program, those sponsors do not bring large numbers of teachers to the U.S. and are not expected to add significantly to the number of visiting teachers in Washington.)

The fiscal impacts of a membership exemption have not been identified for this initial briefing. If the SCPP decides to pursue the proposal, it can direct staff to prepare a bill draft and draft fiscal note.

What Are Some Reasons for a Membership Exemption?

Addresses Administrative Concerns

Visiting international teachers do not remain in the U.S. long enough to become vested in Plan 2 or in the defined benefit portion of Plan 3. Some policy-makers may question whether visiting teachers should be processed as members when they are non-citizens and will not stay long enough to earn a pension.

DRS supports the idea of exempting visiting teachers from membership in TRS 2/3.

The Department of Retirement Systems (DRS) supports the idea of exempting visiting teachers from other countries from retirement system membership. Why? Because visiting teachers would be eligible for refunds upon termination of employment.

DRS has expressed concerns about the administrative impacts of locating individuals who leave the country before requesting to withdraw their member contributions. Tracking people overseas can be difficult, time-consuming, and expensive.

Consistent with Federal Policies

A TRS exemption would be consistent with the federal preference that visiting temporary teachers should not garner assets in this country. The program is designed for visitors, and garnering U.S. assets gives visitors an incentive to remain in the country. This is inconsistent with the premise of the Exchange Visitor Program.

The proposal also supports the federal policies of the U.S. State Department's Exchange Visitor Program by making it easier to attract visiting international teachers. For the teachers themselves, many of whom are required to continue accruing pension benefits in their home country, this approach avoids double pension payments and the complexity of multiple benefits.

Consistent with TRS 1

The membership exemption already exists in TRS 1. An exemption in TRS 2/3 would provide consistency with that Plan.

Visiting Teacher Convenience

The exemption may also be easiest for visiting teachers, as they will not be required to go through an administrative process that is designed for members working toward a pension. The exemption also frees up dollars for teacher expenses while they are in the U.S.

What Are Some Reasons Against the Exemption?

Adds Membership Complexity

The TRS 2/3 membership provisions are inclusive and do not provide special exemptions to other groups of active members working in eligible positions. Adding this exemption adds complexity to the membership provisions.

Currently all teachers who work full time in an "eligible position" must join TRS (unless retired, receiving a disability benefit, or removed from membership for a terminal illness). An eligible position normally requires five or more months of 70 or more hours of compensated employment from September through August. This definition would include visiting teachers under the Exchange Visitor Program.

Spreads UAAL Cost to Non-Participating Employers

Exempting visiting teachers spreads UAAL cost to employers who aren't participating in the VIF Program.

If employer contributions are not collected for visiting teachers because they are exempted from membership, then all TRS employers would experience a small increase in cost for the TRS 1 unfunded actuarial accrued liability, or UAAL. The UAAL is past cost for TRS 1 that is still unpaid. Current funding policy requires that this cost be spread among all TRS employers and collected as a percent of active teacher salaries. If the number of covered teacher salaries decreases by 200-300, the Plan 1 UAAL cost that would have been paid by employers for those teachers must be spread to remaining employers.

Eliminates a Mandatory Savings Plan for Visiting Teachers

Finally, from the perspective of visiting teachers, the membership exemption eliminates a mandatory savings plan that could benefit them they after they leave employment in the U.S. For those who do not accrue pension benefits in their home country while participating in the Exchange Visitor Program, the loss of these savings is more significant.

Impacts Would Reach Beyond the Pension System

Some impacts of this issue reach beyond the pension system. For this reason, it may be desirable for other groups and legislative committees to weigh in on the decision.

The retirement system membership exemption is a factor in VIF's decision to come to a state. Once it initiates the program, a number of positions that are currently filled by U.S. teachers would be filled by teachers from other countries.

The membership exemption helps facilitate the VIF program. The exemption frees up dollars for recruiting, screening, and supporting international teachers - services that most school districts cannot undertake to independently provide. (Examples include interest-free start-up loans to teachers, leased cars, health insurance coverage, visa services, orientation, and on-going problem solving.) VIF provides these services for a fee that is paid by school districts. The dollars that would have been paid for pension contributions are paid to the sponsor. Because the exemption helps facilitate sponsorship of visiting teachers, those who favor this type of cultural exchange program for Washington's public schools would presumably favor the exemption.

For those who do not wish to see an expanded program for visiting international teachers in Washington, a membership exemption may be objectionable. Some may prefer that as many Washington teacher positions as possible remain available to U.S. teachers. There may be concerns that a membership exemption would encourage the program to grow and therefore should not be pursued, especially in times of economic downturn.

Conclusion

There are pros and cons to exempting visiting teachers from TRS membership. Some reasons to support a membership exemption include: administrative concerns with refunds, consistency with federal policies, consistency with TRS Plan 1 and practices in participating peer states, and visiting teacher convenience. Some reasons against the exemption are: adding membership complexity, spreading Plan 1 UAAL costs to other TRS employers who are not participating in the program, and eliminating a mandatory savings plan for visiting teachers. Policy makers will weigh the significance of these pros and cons.

The impacts of a retirement system membership exclusion for visiting teachers from other countries reach beyond the pension system. It may be desirable for other groups and legislative committees to consider those impacts and weigh in on the decision.

Possible SCPP Strategies

1. **Sponsor.** Move the proposal forward as potential SCPP request legislation.

2. **Endorse.** Move the issue forward as potential SCPP endorsed legislation.
3. **Request further study.** Move the issue forward for further study.
4. **Monitor.** Monitor the issue for possible future action.
5. **No action.** Take no action and treat the matter as information only.

Stakeholder Input

Letters from the CEO and Director of Government Relations for the VIF Program are attached.

Next Steps

The Executive Committee will consider the strategies listed and decide whether to direct staff to provide a bill draft and draft fiscal note.

Supporting Information

The attached Fact Sheet was submitted by the VIF Program.

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Post Office Box 3566 • Chapel Hill, NC 27515 • USA • phone 919.967.5144 • fax 919.967.8224 • www.vifprogram.com

Fact Sheet

The Visiting International Faculty Program is the United States' largest international-exchange program for U.S. schools and teachers worldwide. VIF searches the globe for the finest educators to serve as full-time classroom teachers and cultural ambassadors, providing a new generation with an international education to succeed in the global marketplace.

Designated as an official sponsor in the U.S. State Department's Exchange Visitor Program, VIF carefully selects highly qualified teachers from more than 50 nations, matches them with U.S. schools and provides comprehensive support to help ensure a rewarding experience.

VIF provides teachers the professional-development experience of teaching in the United States for up to 3 years before returning home to serve as goodwill ambassadors for the U.S. Since 1989, more than 8,000 VIF teachers have positively influenced the lives of more than a million students, educators and community members.

Some key facts about VIF:

- VIF is the largest international-exchange program for U.S. schools and teachers worldwide. This school year, VIF is sponsoring 1,500 highly qualified teachers in 1,000 schools.
- Teachers serve with VIF for 1 to 3 years and return home to share their experiences with students and colleagues, contributing to education in their nations and to a better understanding of the U.S. abroad.
- VIF's thorough selection process includes a detailed application with essays, verification of credentials and experience, professional references, criminal-background checks and personal interviews. VIF is highly selective, placing only 7% of applicants in U.S. schools.
- VIF teachers must be proficient in English, hold a university degree or teaching diploma equivalent to a U.S. bachelor's degree in education, and have had teacher training and experience at the elementary or secondary level.
- VIF's comprehensive support helps ensure a rewarding experience. VIF teachers and host principals are highly satisfied, independent surveys show: 98% of VIF alumni would recommend VIF to a fellow teacher, and school districts rate their VIF teachers as a 9 on a 10-point scale.
- Schools in several U.S. states participate with VIF, including North Carolina, Georgia, Virginia, South Carolina and Florida.
- VIF educators teach more than 20 subjects, including elementary education, a variety of languages, English as a second language, math, science, special education and many more.
- VIF teachers represent over 50 nations, including Argentina, Australia, Canada, Colombia, Costa Rica, Denmark, Ecuador, France, Germany, Ireland, Jamaica, Mexico, New Zealand, Peru, the Philippines, South Africa, Spain, the United Kingdom and Venezuela.

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November 5, 2008

The Honorable Mark Schoesler
Chairman, Select Committee on Pension Policy
P.O. Box 40409
Olympia, WA 98504-0409

RE: TRS 2 and 3 Exemption Request/Exchange Teachers

Dear Chairman Schoesler and Members of the Committee,

I am writing on behalf of the Visiting International Faculty Program (VIF) of the Center for International Education, Inc. (Exchange Visitor Program P-4-10082). We hope to make Washington a viable location for J-1 exchange teachers by obtaining an exemption from the TRS Plans 2 and 3. As you have already received information on our request in a letter from Mary Donny, I would like to take this opportunity to tell you more about our organization.

The VIF Program is the largest J-1 international teacher exchange program in the United States and is designated as an exchange visitor program sponsor by the US Department of State. Since 1989, VIF teachers have transformed the educational experience of American students, invigorating their schools and communities with meaningful encounters. Participating teachers have been highly successful, succeeding at a rate of around 96%. Many have won school-wide, district-wide and statewide awards. The result has been both excellent instruction and daily intercultural interaction for tens of thousands of U.S. students over the past two decades. This year we are hosting over 1500 teachers from 50 different countries. The teachers are working in 7 states including California, Florida, Virginia, North and South Carolina, Virginia and Georgia. Our exchange educators teach at all levels and subjects in elementary and secondary schools.

The VIF Program follows a rigorous recruiting and selection process to choose the best international educators. Our teachers must not only be excellent instructors but also great cultural ambassadors. We match the teachers with selected host schools, and continuously assist both teachers and schools with comprehensive support services including a call center, mentoring programs, professional development, social events and university partnerships for master's degree programs. VIF provides a turnkey approach to the teachers and schools, facilitating the success of the teachers so their students can reach their potential in their classrooms. In addition, our teachers meet state certification and licensure requirements and are deemed "highly qualified" under the *No Child Left Behind* statute.

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In order to meet the J-1 regulation requirements, we appreciate your consideration of our exchange teacher exemption request. I would be happy to provide you with any additional information or documentation you may require.

Sincerely,

David B. Young
Chief Executive Officer

Post Office Box 3566 • Chapel Hill, NC 27515 • USA • phone 919.967.5144 • fax 919.967.8224 • www.vifprogram.com

September 18, 2008

The Honorable Mark Schoesler
Chair
The Honorable Steve Conway
Select Committee on Pension Policy
The Office of the State Actuary
P.O. Box 40914
Olympia, WA 98504-0914

Dear Mr. Chair, Mr. Vice Chair and Members of the SCPP,

I am writing on behalf of the Visiting International Faculty Program (VIF) d/b/a the Center for International Education, Inc. currently, the VIF Program is the largest J-1 international teacher exchange program in the United States and is a sponsoring agency as designated by the US Department of State (Exchange Visitor Program P-4-10082).

Since 1989, VIF teachers have transformed the educational experience of American students, invigorating their schools and communities with meaningful encounters. Participating teachers have been highly successful, succeeding at a rate of around 96%. Many have won school-wide, district-wide and statewide awards. The result has been both excellent instruction and daily intercultural interaction for tens of thousands of U.S. students. Last year we hosted over 1650 teachers from 50 different countries and placed them in 7 states including Maryland, Virginia, North Carolina, South Carolina, Georgia, Florida and California.

Before we begin to bring our teachers to a specific state, we work to make sure that there are no regulatory or statutory barriers that would prevent exchange teachers from working in the state. Over the past few years, we have been approached by several school districts requesting VIF to bring our international exchange teachers to Washington. We believe international teachers would find the state of Washington an attractive location to serve as highly qualified educators and cultural ambassadors.

As you may be aware, under the federal J-1 teacher regulations as written in 22 CFR 62.24, there is a subdivision that notes that while the teachers may take a full-time position, they are here on a temporary (non-immigrant) basis. Specifically, the regulations outline the following in 22 CFR 62.24 2 (e) *Teaching position. …The exchange visitor's appointment to a position at a primary or secondary accredited educational institution shall be temporary, even if the teaching position is permanent.* Our government prefers that the teachers not garner assets while they are here in the US. In fact, some of our exchange teachers are granted leave from their home countries and continue to receive pension credits (civil servant status) while they are in the US on our exchange program. At this time, all the states in which we work, except Maryland, exclude exchange teachers from participation in their retirement systems. (We have not yet asked to be excluded from Maryland's system at this time for non-related reasons).

I am therefore writing to request an exemption from the TRS Plans 2 and 3 on behalf of J-1 exchange teachers. We have been touch with the Washington Teachers' Retirement System (Jeff Wickman and Sandra J. Matheson) regarding this issue. They have indicated that while there is an exception to TRS 1 for "alien" teachers, there is no such exemption to TRS Plans 2 and 3 and that a legislative remedy is required.
The TRS Plan 1 language in RCW 41.32.240 states….(1) *All teachers employed full time in the public schools shall be members of the system except alien teachers who have been granted a temporary permit to teach as exchange teachers.* Given that there is precedence for an exemption, we ask your consideration of extending that exemption to TRS Plans 2 and 3.

Thank you for your review of our request. I am happy to address any questions you may have or provide any additional information you may require.

Sincerely,

Mary Donny
Director of Government Relations

The Select Committee on Pension Policy

Visiting International Faculty

Laura Harper, Policy and Research Services Manager
November 18, 2008

Office of the State Actuary
"Securing tomorrow's pensions today."

A New Issue For This Interim

- Should visiting teachers from other countries be exempt from retirement system membership?
  - Issue brought to you as a stakeholder request
  - Request comes from the Visiting International Faculty Program (VIF)
- First briefing of interim
  - Background on VIF
  - Policy pros and cons
  - Possible strategies or next steps

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"Securing tomorrow's pensions today."
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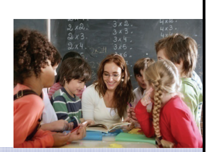
What Is VIF?

- VIF sponsors teachers from other nations under the U.S. Department of State's Exchange Visitor Program
  - Largest sponsor in U.S.
  - Significant presence in seven states
- Program promotes educational and cultural exchanges
  - Teachers work full-time for one to three years
  - Teachers must obtain a special visa

Why A Membership Exemption?

- Facilitates the program
  - Frees up dollars for sponsor services
  - Makes program roughly cost-neutral for school districts
- Preferred by U.S. Department of State
  - Avoids having visitors garner U.S. assets
- VIF typically requests membership exemption before bringing its program to a state



What Is The Current Situation?

- TRS 1 already has the membership exemption
  - Closed plan
- In TRS 2/3, full-time visiting teachers must become members
  - Pay contributions even if they will not vest in a pension
  - Apply for refund when leave employment
  - Employer contributions remain with TRS
- Statutory change is needed to exempt these teachers from membership

What Do Other States Do?

- Two peer states participate in VIF
  - Both provide membership exemption
    - Florida requires temporary visa and three-year time limit
    - California has broad exemption
- Five other states participate
  - Four of five provide membership exemption

How Would This Exemption Impact TRS?

- Plan administration
  - Department would not collect member or employer contributions
  - No service credit would accrue for these members
  - No refunds of member contributions would be paid after visiting teachers leave employment
- Number of TRS positions affected
  - Potentially twenty in first year of program (2010-2011)
  - Could grow to 200-300 when at full capacity

Policy Pros And Cons…

Reasons For

- Addresses DRS concerns
- Consistent with federal policy
- Consistent with TRS 1
- Consistent with peer states
- Visiting teacher convenience

Reasons Against

- Adds membership complexity
- Spreads Plan 1 UAAL cost to other employers
- Eliminates a mandatory savings plan

Impacts Reach Beyond The Pension System

- Membership exemption is a factor in bringing VIF to a state
  - Once VIF comes in, as many as 200-300 positions could be affected
- Raises questions for other groups
  - Desirability of program from educational perspective?
  - Desirability of program from a cultural perspective?
  - Trade-offs for filling positions with non-U.S. teachers?

There Is A Range Of Possible Strategies

- Sponsor
  - Direct staff to bring back bill draft and draft fiscal note
  - Hold public hearing
- Endorse
  - Make a record by voting on a motion
- Request further study
- Monitor
- Take no action

4. Change Membership Default for Plans 2/3

Change Membership Default For Plans 2/3

Description of Issue

The SCPP is being asked to change the plan choice default in the Plans 2/3 of the Public Employees' Retirement System (PERS), Teachers' Retirement System (TRS), and the School Employees' Retirement System (SERS). The requested change would require new employees who failed to choose Plan 2 or Plan 3 to become permanent members of Plan 2 by default. The current default plan is Plan 3.

This request raises two immediate policy questions:

- Should the plan default be changed, particularly at this time?
- If so, how should the default be determined?

History

- Plan 3 was the default plan when plan choice was introduced with PERS Plan 3 in 2002.
- The Legislature continued to use Plan 3 as the default when new teachers and school employees were granted plan choice in 2007.

Policy Considerations

- Have the values changed that made the Plan 3 design the policy preference for the default plan?
- There may be issues with changing the default at this time.
    - Legal considerations.
    - Financial market conditions.
- If policy makers don't have a policy preference for continuing the Plan 3 default, how should they decide which plan should be the default?
    - Look at historical data of plan choice preference?

   - Determine which plan best serves the needs of new employees?

What is the Next Step?

The committee has several options to consider.

- Take no action at this time, given the timing of the request.
- Study additional options for the default. This could involve further demographic analysis of the new employees in each plan.
- Move the issue forward for further public hearing and analysis.

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Change Membership Default for Plans 2/3

In Brief

ISSUE

New employees hired into PERS, TRS, or SERS eligible positions must choose to be a member of Plan 2 or Plan 3. Members who don't choose are "defaulted" into membership in Plan 3. Stakeholders have suggested that members who don't choose should be defaulted into Plan 2.

MEMBER IMPACT

This change would impact all new hires into PERS, TRS, and SERS eligible positions. Since the inception of optional membership, beginning for PERS in March 2002, over 95,000 new employees have been faced with the Plan 2 or Plan 3 choice. Of these, nearly 18,000 have been defaulted into Plan 3. See Appendix A for more information.

Dave Nelsen
Senior Policy Analyst
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Introduction

The SCPP is being asked to change the optional plan choice default provisions in the Plans 2/3 of the Public Employees' Retirement System (PERS), the Teachers' Retirement System (TRS), and the School Employees' Retirement System (SERS). The requested change would require new employees who failed to choose Plan 2 or Plan 3 to become permanent members of Plan 2 by default. Currently, new employees who fail to choose a plan are permanently defaulted into membership in Plan 3. This request raises two immediate policy questions:

- ❖ Should the plan default be changed, particularly at this time?
- ❖ If so, how should the default be determined?

Current Situation

New employees hired into eligible positions in PERS, TRS, and SERS have ninety days from their first day of employment to choose whether to become members of Plan 2 or Plan 3. New employees who do not decide within the ninety-day window become members of Plan 3 by default. Whether members choose or are defaulted into a plan, their plan designation cannot change; the decision or designation is irrevocable.

History

TRS Plan 3, implemented in 1995, was the first Plan 3 in Washington State. At the time, all new teachers were required to be members of Plan 3. This was also true for SERS Plan 3, implemented in 2000. Classified employees hired after 2000 were also required to become members of SERS Plan 3.

The choice of Plan 3 as the default plan began with the implementation of PERS Plan 3 in March 2002. When PERS Plan 3 was created, the Legislature gave new public

Using Plan 3 as the default plan started with PERS in 2002 and was later expanded to TRS and SERS in 2007.

employees the irrevocable choice upon hiring to become a member of Plan 2 or Plan 3. If a new employee failed to make a choice, they were defaulted into PERS Plan 3.

In 2007, the Legislature continued to use Plan 3 as the default plan when they implemented optional membership in TRS and SERS. These benefits, and others, were passed in HB 2391, which also repealed the provisions of gain-sharing. Some of the provisions of this bill are currently being litigated.

Comparing Plan 2 and Plan 3

Plan 2 and Plan 3 provide different designs to accrue a retirement benefit. Understanding the differences in the design of the two plans may help policy makers understand the potential impact of changing the default plan to future new employees.

Below is a description of the benefit design provided by each plan.

Plan 2 is a defined benefit plan that provides a monthly payment for life based upon a formula.

Plan 2 is a **defined benefit retirement plan** that provides a monthly payment for life based upon a formula. The benefit is defined because the formula is known. The Plan 2 benefit formula is: 2% X years of service X salary average. The Plan 2 benefit is funded by equal employee and employer contributions, which may vary over time depending upon the funding needs of the plan. The full benefit is guaranteed by the state of Washington, so employees do not carry the investment risk for their benefits, the state does.

Some Benefits of Plan 2

For a new employee who will remain a member until retirement, DB plans, like the Plans 2, are generally a very cost effective method to provide lifetime retirement income.*

First, because they "pool" all members into a common fund, defined benefit plans only have to collect enough contributions and earnings to fund the "average" lifetime of the member. Members who fund their own retirement would have to contribute and earn more in order to ensure

Plan 2 offers a cost effective method to provide replacement income at retirement.

they wouldn't outlive their savings if they lived longer than the average.

Second, because large defined benefit plans invest over a very long time horizon, they can afford to take on more investment risk, which should lead to higher returns. Individual members are often advised to change their investment allocations to less risky products as they near and enter retirement, which leads to lower lifetime investment returns.

Finally, defined benefit plans generally achieve higher investment returns than individual investors. Defined benefit plans use investment professionals, have access to investment asset classes that individuals typically don't, and can use their size to negotiate lower investment fees. Over a long career, a small increase in investment returns can provide a significantly higher benefit.

** "A Better Bang for the Buck" by Beth Almeida and William Fornia, FSA August 2008*

Plan 2 offers members a lower risk retirement plan that requires little involvement in managing the benefit.

Plan 2 is also of value to members who don't want to assume the primary responsibility and risk for their own retirement funding. In a defined benefit plan, the plan sponsor assumes the responsibility and the risk to invest and provide a retirement benefit for the employees. This provides the member with a secure, known benefit that is guaranteed. For members who lack the investment confidence, the desire to more directly manage their retirement income, or the time to accrue substantial earnings, this option can be desirable. However, members do still bear the responsibility to determine if the amount provided by the plan is sufficient for their own retirement needs, and make additional plans if it is not.

Plan 3 is a **hybrid retirement plan**, because it contains two separate components:

- ❖ A defined contribution account.
- ❖ A defined benefit account.

The *defined contribution* account is funded by the member's own contributions. The plan gives members the choice of how much they want to contribute to their own retirement, and options to manage investing those contributions over time. Currently, Plan 3 members have six contribution rate options, beginning at 5 percent, and over nine separate investment funds from which to choose.

New employees, who become members of Plan 3 by default, are also defaulted into a contribution rate of 5 percent and into an investment option that provides the same mix of investments and rate of return as the retirement trust funds managed by the Washington State Investment Board (WSIB).

Plan 3 has both a defined contribution and defined benefit component.

This is called a "defined contribution" account because the benefit received by members from the account is not defined, only the amount of contributions into the account is defined. The benefit received from the account is based upon how much members contribute and the associated investment earnings. There is no guaranteed return on the contributions, so members carry the full investment risk. This type of retirement option is very similar to the "401K" retirement plans commonly offered by private employers.

The *defined benefit* account in Plan 3 is paid by the employer contributions. The defined benefit provided is similar to the Plan 2 defined benefit, a lifetime monthly payment based upon a formula, guaranteed by the state. However, because member contributions are not funding the defined benefit in Plan 3 like they are in Plan 2, the value is half that of the Plan 2 benefit. The Plan 3 defined benefit formula is: 1% X years of service X salary average.

Some Benefits of Plan 3

Plan 3 offers members more value if leaving the workforce before retiring.

Many new employees will never draw a lifetime monthly payment from their retirement plan. It is estimated that less than half of all new PERS employees will remain employed for the five years necessary to earn a guaranteed benefit at age 65.* Also, some new employees may work long enough to earn a benefit, but will leave public employment prior to age 65. The Plans 3 were designed in recognition of this new, more mobile workforce. The policy statement in the legislation that created TRS Plan 3 stated "...public employees need the ability to make transitions to other private or public sector careers, and ... the retirement system should not be a barrier...."

To accommodate this recognition of greater mobility, Plan 3 provides more opportunity to receive value for both member and employer contributions should employees leave employment prior to retirement. In Plan 2, members who leave employment can withdraw the contributions made to the plan and any interest that has been credited to their account. However, if they do so, they forfeit all right to a future defined benefit from the system. This means Plan 2 members who withdraw never receive any benefit from all the contributions made by the employer.

In Plan 3, the benefit is split into the defined contribution and the defined benefit accounts. Plan 3 members who leave prior to retirement can withdraw their contributions from the defined contribution account, and it does not impact their eligibility for an employer-funded defined benefit payment in the future. If Plan 3 members earn a guaranteed future payment, they retain the value from the employer contributions.

** 2007 Actuarial Valuation Report, OSA, September 2008.*

Plan 3 gives members greater flexibility and control within their retirement plan.

Plan 3 also offers members more control over their retirement planning. With the increased awareness of the stock market in the late 1980s and early 1990s, many employees wanted flexibility and control over their retirement contributions. Plan 3 provides flexibility in the amount of contributions and control over how they are invested. Plan 2 does not provide these benefits. Even if the new employees do not choose Plan 3 initially, this flexibility and control may be desired later in their career.

However, with this increased flexibility and control comes increased risk. Members in Plan 3 are assuming more risk for their future retirement benefit than Plan 2 members. Part of the benefit from Plan 3 comes from the members own contributions and earnings, on which there is no guaranteed return. Therefore, depending upon the amount invested and the earnings, members may or may not have as much income replacement at retirement as Plan 2 members may have.

Plan 3 shifts some risk of providing a retirement benefit to members, but provides features to help mitigate that risk.

Some policy makers may question whether a plan designed for active management that shifts some retirement risk to members is appropriate for new employees who cannot choose a retirement plan in ninety days. While there is more risk to members in this plan, there are several design options within Plan 3 that attempt to mitigate some of that risk.

First, as stated earlier, members who are defaulted into Plan 3 are also defaulted into the WSIB investment option. This provides them with access to a professionally managed, low-fee, and diverse investment portfolio, the same portfolio that funds the defined benefit plans in Washington. This option mitigates some of the risk for individual investors.

Second, the Plans 3 provide an option for members to purchase a lifetime monthly annuity with their contributions at the time of retirement, paid out of the state retirement funds. Because this annuity is purchased from the state, it provides more benefit for less cost than what could typically be purchased in the private sector, and removes some of the risk of members outliving the value of their investments.

Finally, members still receive a defined benefit payment funded from the employer contributions. This ensures there is some level of secure monthly income being earned.

Policy Analysis

The request to change the plan membership default in the Plans 2/3 raises two immediate policy questions:

- Should the default be changed, particularly at this time?
- If so, how should the default be determined?

Should the Plan Default Be Changed?

As discussed earlier in this paper, Plan 3 was the original choice as the default plan for PERS, and has remained the default choice as optional membership was expanded to TRS and SERS. As shown in **Appendix A**, nearly 18,000 members have been defaulted into Plan 3 since the creation of optional membership. This amounts to approximately 19 percent of all new employees.

The question for policy makers is: Have the values changed that made the Plan 3 design the policy preference for the default plan?

The Plan 3 design offers value for the mobility and flexible retirement planning needs of many new employees. For employers, it offers a retirement plan that helps recruit from the private sector, which primarily offers defined

Have the values changed that made the Plan 3 design the policy preference for the default plan?

contribution retirement plans for employees. For the state of Washington, as the plan sponsor, the Plan 3 design shifts some of the investment risk for providing a benefit to members, and lowers the long-term cost of the plan that the state guarantees. As explained earlier, the Plan 3 members carry the investment risk for their own contributions, and the state guarantees the value of the defined benefits paid by employer contributions. Since the Plan 3 defined benefit is half the value of the Plan 2 defined benefit, the state accrues less liability with Plan 3. Shifting the investment risk and lowering the long-term liability were key benefits to the state of implementing Plan 3 and designating Plan 3 as the default plan.

Have the values in the Plan 3 design changed? Do policy makers no longer consider lowering the long-term liability for the state a goal? If the values discussed above have not changed, then some reason must override the design values in significance to consider changing the current plan default. Otherwise, retaining Plan 3 as the default plan would be the consistent approach.

Should the Default Be Changed at this Time?

Changing the plan default at this time may raise legal concerns.

In addition to the question of whether the Plan 3 default should be changed at all, there are also two concerns raised by the timing of this request. First, as mentioned earlier, the legislature continued the use of Plan 3 as the default plan when they implemented plan choice for TRS and SERS in HB 2391. Some of the benefit provisions in this bill are in current litigation, and the provisions of plan choice may be impacted by the outcome of this litigation. As a result, the committee may want to consult with their Assistant Attorney General before making a decision on this proposal.

Second, policy makers may want to consider whether the desire to change Plan 3 as the default may be linked to current market conditions. As discussed earlier, in Plan 3 members invest their contributions. When the financial markets are in a downturn, as they are now, the reaction to this financial climate may be that this exposure to investment risk is too great for members to accommodate. Therefore, some feel Plan 2 should be the default plan because the benefit is guaranteed and the state, as plan sponsor, should carry the investment risk, not members. This

Policy makers may want to consider whether the desire to change the default from Plan 3 may be linked to current market conditions.

reaction may not fully consider the cyclical nature of the financial markets. The markets have had periods of tremendous gain, as well as loss. Volatility is part of their nature. When the financial markets are earning significant returns, will there be another request to change the default back to Plan 3 so members can participate in the gains?

How Should the Plan Default Be Determined?

If policy makers no longer feel Plan 3 should be the default plan for new employees from a broad-based policy perspective, then how should they choose which plan should be the default? Two possible approaches are:

- Use historical plan choice data to set the default.
- Determine which plan best serves the needs of new employees.

Using Historical Data to Set Plan Default

Appendix A provides detail of new employee choice in the Plans 2/3. PERS has had optional membership since March of 2002, so there is more historical data available. In PERS, over 64 percent of new employees choose Plan 2. An additional 17 percent choose Plan 2, and the remaining 19 percent are defaulted into Plan 3. This data indicates a strong preference in PERS for Plan 2.

SERS data also indicates a preference for Plan 2 of 48 percent to 32 percent choosing Plan 3. The remaining 20 percent are defaulted into Plan 3. TRS new members have a slight preference for Plan 3 of 46 to 40 percent choosing Plan 2. The remaining 14 percent of new teachers are defaulted to Plan 3.

Historical data shows a strong preference for Plan 2 among PERS employees, but the data is somewhat less clear for school employees and teachers.

While this data does show a strong preference for Plan 2 among PERS employees, the data is somewhat less clear for school employees and teachers. Also, since optional membership for SERS and TRS was implemented only 16 months ago, there is far less data in those plans from which to base a decision. If taking the approach to use historical data to determine the plan default choice, policy makers may want to consider whether enough data is available in SERS and TRS to make an informed choice.

Which Plan Best Serves the New Employees?

Policy makers may also set the plan default based upon a judgment of which plan best serves the new employees. This determination is complicated; however, as Plan 2 and Plan 3 were each designed to best serve the needs of different members. As discussed earlier in this paper when comparing the benefits in the two plans, Plan 2 may provide more value to the new employees who stay and retire from the system, or who don't want the primary responsibility or the risk of managing their own retirement. Plan 3 may be preferable for the new employees who will likely leave public employment prior to retirement, or those who may remain, but want more flexibility and options than a typical defined benefit plan provides.

Policy makers would need to determine which group of new members they would like to best serve. Those new employees who will stay to retirement age may be benefited by a Plan 2 default, and those who leave prior to retiring may be benefited by a Plan 3 default.

Should There Be Different Defaults for Different Members?

Instead of one default for all retirement systems, other approaches could include defaults based upon each system's demographics, or plan default based upon groupings of new employees.

Applying one default plan for all the Plans 2/3 would necessarily mean some members are defaulted into a plan that may not be best suited for their needs. A different approach may be to fit the default to the demographics of new employees in the retirement system. For example, PERS and SERS new employees are far more likely to leave the workforce prior to the normal age of retirement than new TRS employees. Would a Plan 3 default suit these employees better since it may provide more value to a departing worker? If new employees in TRS are more likely to work to the normal age of retirement, should they be given a Plan 2 default since Plan 2 is a cost effective means of providing retirement income? This approach could result in different default plans among the three retirement systems.

Another approach would be to fit the default to groupings of new employees specifically. For example, Plan 3 may be more valuable to younger employees who have time to invest and manage their contributions through market volatility. Plan 3 may be a logical choice as the default for these new employees. But what of new employees that enter the workforce at later ages? They may not have time to earn significant investment gains in Plan 3. New employees past a certain age may benefit from being defaulted into Plan 2. This approach could result in different plan defaults within each retirement system.

Other States

Among the comparative states, only two systems offer new employees a choice between a defined benefit plan and some form of defined contribution or hybrid plan, Ohio PERS and the Florida Retirement System.

Only two comparative systems offer similar plan choice to new employees, and both systems default members into the defined benefit option.

Ohio PERS gives new employees a choice between a traditional defined benefit plan like Plan 2, a hybrid retirement plan like Plan 3, and a defined contribution plan. If members do not choose a plan, they are defaulted into the traditional defined benefit plan.

The Florida Retirement System gives new members the option to participate in a defined benefit plan and a defined contribution plan. Like Ohio PERS, if members fail to make a timely choice, they are defaulted into the defined benefit plan.

Conclusion

There is a request to the SCPP to change the plan choice default in the Plans 2/3. Plan 3 has been the policy choice as the plan default since the inception of optional membership in 2002, and remained the default choice when optional membership was expanded in 2007. Have the plan design values that drove that default policy changed?

Is now the right time to change the plan default? There are also timing considerations concerning changing the plan default. These include possible legal concerns and the impact of the current financial markets on the desire for change.

If policy makers don't have a policy preference for continuing the use of Plan 3 as the default, how should they determine which plan should be the default?

- Look at historical data of plan choice preference?

- Make a determination of which plan best serves the needs of new employees?

A look at similar situations in comparative state systems shows that only two systems offer new employees a similar plan choice as Washington. In both of those systems, members who fail to choose within their allotted time period are defaulted into a defined benefit plan.

What is the Next Step?

The committee has several options to consider.

- Take no action at this time, given the timing of the request.
- Study additional options for the default. This could include further demographic analysis of the new employees in each plan.
- Move the issue forward for further public hearing and analysis.

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Appendix A

PERS Choice Data – March 2002 through October 2008		
New Members	85,106	
New Members Opting Into Plan 2	54,067	64%
New Members Opting Into Plan 3	14,882	17%
New Members Defaulting Into Plan 3	16,157	19%

TRS Choice Data – July 2007 through October 2008		
New Members	5,189	
New Members Opting Into Plan 2	2,072	40%
New Members Opting Into Plan 3	2,387	46%
New Members Defaulting Into Plan 3	730	14%

SERS Choice Data – July 2007 through October 2008		
New Members	5,094	
New Members Opting Into Plan 2	2,443	48%
New Members Opting Into Plan 3	1,616	32%
New Members Defaulting Into Plan 3	1,035	20%

The Select Committee on Pension Policy

Change Membership Default in Plans 2/3

Dave Nelsen, Senior Policy Analyst

November 18, 2008

Office of the State Actuary

"Securing tomorrow's pensions today."

What Is The Issue?

- Newly hired employees in PERS, TRS, and SERS who don't choose a plan are put into Plan 3
- An SCPP member requested that the committee study changing the plan choice default to Plan 2
- Is the current default still the preference of policy makers?

Today's Briefing

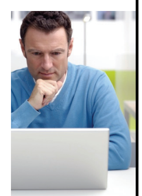
- Work session
  - Background on default provision
  - How change may impact members
  - Key policy questions on changing the default

Background

- New employees in PERS, TRS, and SERS have 90 days to choose a plan
  - Defaulted to Plan 3 if they don't make a choice
    - Minimum rate option (5%)
    - Contributions managed by WSIB
  - Plan membership is permanent, whether chosen or defaulted
- Plan 3 was original default plan
  - PERS in 2002
  - TRS and SERS in 2007
  - 18,000 new employees have defaulted into Plan 3

How Would Change Impact Members?

- Each plan designed to meet different needs
  - Plan 2
    - Defined benefit plan
    - Career employee
    - Little member risk or control
  - Plan 3
    - Hybrid plan
      - Defined contribution account
      - Defined benefit
    - Mobile employee
    - More member control and involvement
    - More member risk



Key Policy Questions

- Should the Plans 2/3 membership default be changed?
- Should the default be changed at this time?
- If so, how should policy makers decide which plan should be the default plan?

Why Was Plan 3 The Default Plan?

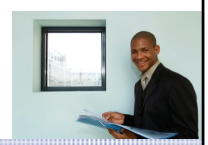
- Choice likely based upon the values in the Plan 3 design
- Value for new workforce
  - Flexibility and control
  - Career mobility
- Less long-term liability and risk for the state
  - Guaranteed benefit only half of Plan 2 amount
- Have the values behind the original choice of default changed?

Is Now The Right Time To Change?

- Possible legal concerns
  - TRS and SERS default part of plan choice created in HB 2391
- Linked to financial market concerns?
  - What happens when markets increase?

How Should The Default Plan Be Determined?

- Use historical plan choice data
- Use plan design features to decide which plan best serves needs of new employees



Plan Choice Data

- Data shows a strong preference for Plan 2 in PERS
- Less clear for TRS and SERS

	PERS*		TRS**		SERS**	
New Members	85,106		5,189		5,094	
Opting Into Plan 2	54,067	64%	2,072	40%	2,443	48%
Opting Into Plan 3	14,882	17%	2,387	46%	1,616	32%
Defaulted Into Plan 3	16,157	19%	730	14%	1,035	20%

**Data from March of 2002 through October 2008.*
***Data from July 2007 through October 2008.*

Match Plan Default With Needs Of Members

- Each plan designed to meet different needs
- Several Options
  - One default for all systems
  - System specific default
    - Each system's demographics drive default choice
  - Default based upon new employee demographics
    - Employee categories drive default choice

Other States

- Two comparative systems provide similar plan choice to new employees
  - Ohio PERS
  - Florida Retirement System
- Both systems default new employees to a defined benefit plan

In Summary…

- Have the values changed that set Plan 3 as the default?
- Is now the right time to change?
  - Legal concerns
  - Market conditions
- How should the default be chosen?
  - Use historical data
  - Use plan design features to decide which plan best meets needs

Next Steps

- Take no action
- Study additional options
- Move the issue forward

5. Interruptive Military Service Credit

Interruptive Military Service Credit

Description of Issue

Should members receive free service credit for periods of public employment that are interrupted by military service during a period of war?

After studying this issue in 2007, the SCPP answered yes and proposed a bill to add this benefit to the open plans (Plans 2 and 3). In the 2008 session SSB 6645 passed Senate Ways and Means but was not heard in the House.

The LEOFF 2 Board asked the SCPP to consider this issue again this interim and to examine more closely how the benefit would be applied.

Options for Applying the Benefit

1. Apply only to service after the effective date of the bill (prospective).
2. Apply to service credit transactions after the effective date of the bill, whether or not some or all of the service was before the bill's effective date (last year's SCPP-sponsored bill). No refunds would be paid under this option.
3. Apply to all service – past, present and future - with refunds for all service previously purchased for ongoing designated conflicts (Operation Iraqi Freedom and Operation Enduring Freedom, including Afghanistan).
4. Apply to all service – past, present and future - with refunds for all service credit previously purchased for service during a period of war.

Preliminary pricing for Options 2, 3 and 4 will be provided at the November 18, 2008 meeting.

Other Materials Included

- SCPP Issue Paper
- Copy of statutory definition of "period of war," RCW 41.04.005(2)
- Stakeholder correspondence from LEOFF 2 Board

What is the Next Step?

Members will decide whether to sponsor a bill in the 2009 session, and if so, how the benefit should be applied. If so directed, staff will prepare a new bill draft and draft fiscal note.

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Interruptive Military Service Credit

In Brief

ISSUE

Should members receive free service credit for periods of public employment that were interrupted by military service during a period of war? If so, should this benefit be applied to past service? Should members who already paid to reinstate past service receive refunds?

MEMBER IMPACT

All active members of the open plans in all systems could potentially be impacted, since all plans provide for interruptive military service credit. OSA's 2008 fiscal note for SSB 6645 estimated that one out of 4,700 members could be impacted by this proposal in a given year.

Laura Harper
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Current Situation

"Interruptive military service" includes the following:

- The member leaves public employment to serve in the uniformed services.
- The service is honorable.
- The member returns to public employment upon completion of the service.

Employment practices related to interruptive military service are governed by federal law. At a minimum, public employers must provide their members with the protections specified in the Uniformed Services Employment and Re-employment Rights Act (USERRA). Included in USERRA's re-employment rights is the right to restore retirement plan benefits such as service credit.

Currently, to reinstate service credit for interruptive military service completed on or after October 6, 1994, a member must pay employee contributions (no interest). If the service was completed on or after March 31, 1992, and before October 6, 1994, the member must pay the employee contributions plus interest. For interruptive military service completed on or after October 1, 1977, and before March 31, 1992, the member must pay both the employer and employee contributions plus interest.

A member who cannot return to public employment due to a total disability must also repay contributions to receive interruptive military service credit. In the case of a military death, the member's survivor can pay what would have been the member cost to receive the service credit.

Generally, members must make the required payments within five years of resuming service with their employer, or prior to retirement, whichever comes first. Members who fail to make timely payment have the option of purchasing the service credit by paying the actuarial cost of the resulting increase in their benefits. Survivors must pay the member cost within five years or prior to receiving a benefit.

When the benefit is more generous than what USERRA provides, the legislature can set parameters for granting the benefit.

The state can be more generous to members than required by USERRA if it so chooses. For example, the Legislature may choose to provide free service credit for members whose public employment is interrupted by military service during a period of war. When the benefit is more generous than what is already provided under federal law, the Legislature can set its own parameters for granting the additional benefit.

Example A

A member voluntarily joins the armed forces during peace time. The member's military service interrupts public employment, and the member serves honorably. The member complies with USERRA and repays contributions. The state retirement system must grant interruptive military service credit to the member.

Example B

The Legislature chooses in an upcoming session to improve benefits. The retirement system already complies with USERRA, but the Legislature decides to amend the retirement plan to provide free interruptive military service credit for serving honorably during a period of war. [See RCW 41.04.005(2), attached, which defines "period of war."] With such an amendment in place, a plan member can apply for **free** service credit for those periods of interruptive military service that are defined in **state** law. The parameters for granting free service credit (Example B) are more strict than those for granting standard interruptive military service credit (Example A).

History

The SCPP first studied interruptive military service credit in the 2004 interim. At that time, the SCPP concluded that USERRA did not adequately address members who were unable to return to public employment due to a death or total disability while serving in the uniformed services. As a result, the SCPP recommended legislation to address this issue. Chapter 64, Laws of 2005 provided that a member with a total disability or a survivor of a deceased member may purchase service credit for interruptive military service up to the date of death or disability. The law requires repayment of member contributions to reinstate service credit for the period of interruptive military service.

The SCPP also studied interruptive military service in the 2007 interim. The Committee decided that more should be done for retirement system members whose public employment was interrupted by military service during a period of war.

The SCPP recommended a bill for the 2008 legislative session that would have granted free service credit for interruptive military service during a period of war.

The SCPP recommended a bill for the 2008 Legislative session that would grant free service credit for interruptive military service during a period of war. Period of war is defined in RCW 41.04.005(2)(copy attached). The bill was endorsed by the Law Enforcement Officers' and Fire Fighters' Plan 2 Board (LEOFF 2 Board). SSB 6645 (2008) passed Senate Ways and Means and was not heard in the House.

During the current interim, the SCPP received correspondence from the LEOFF 2 Board requesting that the Board and the SCPP work cooperatively to submit a bill in 2009 on this issue. The LEOFF 2 Board seeks to eliminate members' obligation to pay contributions to obtain service credit for interruptive military service during a period of war. The Board identified the issue as priority number three out of five issues for SCPP coordination. The LEOFF 2 Board also requested that the SCPP explore possible retroactive application of the bill.

Policy Analysis

The SCPP Can Give Better Benefits than Those Required by Federal Law.

Interruptive military service is governed by federal law. At a minimum, public employers must provide the protections specified in the USERRA. This law provides for the re-employment of individuals who leave employment to serve in the "uniformed services," a term that is federally defined and includes most types of military service. Included in USERRA's re-employment rights is the right to restoration of retirement plan benefits.

USERRA treats employees as if they had been continuously employed during the period of interruptive military service.

For employers, the fundamental requirement of USERRA as it relates to retirement plan benefits is to provide for recovery of the benefits that a re-employed participant did not receive due to qualifying military service. The employee must be treated for vesting and benefit accrual purposes as if he or she had been continuously employed. Thus, the member must pay the contributions that would have been paid during the period of service, and can receive service credit as if there had been no interruption in employment.

USERRA pre-empts state retirement policy in that all public employers must meet the minimum requirements of this federal law. However as mentioned above, employers have the discretion to go beyond USERRA and grant benefits for periods of interruptive service that are more generous than those available under the act. Employers who choose to go beyond USERRA may do so by using a variety of methods. They can grant free service credit for periods of interruptive military service. They can reward active duty by paying all or part of the contributions that the member would have paid during the period of active duty. Employers may also provide all or part of the member's salary during such periods. Enhanced benefits can be limited to wars and armed conflicts as long as the basic USERRA protections remain intact for all interruptive military service in the uniformed services.

Most of Washington's closed plans provide free interruptive military service credit.

Comparison with Other Washington Plans

Currently, free interruptive military service credit is available to members in most of the closed plans, including Plan 1 of the Public Employees' Retirement System (PERS 1), Plan 1 of the Law Enforcement and Fire Fighters' Retirement System (LEOFF 1), and Plan 1 of the Washington State Patrol Retirement System (WSPRS). This benefit is not available in Plan 1 of the Teachers' Retirement System (TRS).

Comparison with Other States

California, Idaho, Iowa, and Wisconsin provide free interruptive military service credit. None of these states limit free credit to declared wars or armed conflicts.

Ohio allows members to purchase interruptive military service credit under USERRA, and also grants free service credit to members under more restrictive conditions, including requirements that members participate in the retirement system on a contributing basis for one year prior to and one year after the interruptive military service.

Washington's peer states are split on the issue.

Florida is a non-contributory state, meaning members do not contribute to their retirement benefits. Thus, there are no member contributions to repay in order to receive interruptive military service credit under USERRA.

Missouri's plans differ. The State Employees' plan is non-contributory like Florida's. The Public School Plan allows members to purchase service under USERRA. The Local Government Plan provides free interruptive service for USERRA-qualified service.

The remaining states – Colorado, Minnesota, and Oregon – require members to repay contributions.

Reasons For and Against Providing Free Service Credit

The following table summarizes some of the policy pros and cons of providing special or increased benefits to members based on military service:

Free military service credit has pros and cons.

No Additional Special Benefits	Additional Special Benefits
Members serve voluntarily; no draft requires them to leave employment	Encourage military service; help avoid need for a draft
Members already receive adequate federal compensation and benefits for military service	Support ability to recruit more military personnel into state service and more state personnel into military service
Other members and employers would not have to absorb extra costs for these members	Support view that all WA citizens benefit, directly or indirectly, from military service rendered by public employees
More favorable service credit treatment is already given to these members via federal law (no interest, 5 years to repay)	Recognize that members who serve in conflicts are at higher risk for injury or death; pension plans typically offer extra support for high risk occupations that serve the public at large
Military service is unrelated to the service rewarded by state pension plans	Supplement federal benefits, which may not be viewed as adequate

The LEOFF 2 Board asked the SCPP to give additional consideration to how the benefit is applied. Four options are outlined here.

How Should the Benefit Be Applied?

In testimony before the SCPP at its July 15, 2008, meeting, the LEOFF 2 Board's Executive Director asked that the SCPP consider possible retroactive application of the bill. There are several options that policy-makers might choose for determining who would be eligible to receive free interruptive military service credit for periods of war. The options range from a prospective application of the benefit to a retroactive application with refunds.

Option 1 – Prospective Service Only

Under this option, only interruptive military service after the effective date of the bill would be free and credited to members without repayment of member contributions. This approach is the least generous to members of the four options described but is also the least costly. It is the more common approach to benefit improvements, as it allows for contributions to be adjusted along with the implementation of the benefit improvement. This approach is also consistent with principles of intergenerational equity (meaning that each generation of taxpayers should pay only for the benefits associated with the services rendered to that generation of taxpayers). One possible concern with this approach is that service within the same conflict is treated differently – some is free and some is not.

Preliminary pricing for Options 2, 3, and 4 will be provided at the November meeting.

Option 2 – Past and Prospective Service with No Refunds

Under this option, free interruptive military service credit would be available to members who apply for the service credit after the effective date of the bill. Members can apply for interruptive military service credit any time up to their retirement. Thus, active members who have not yet retired could pick up free service credit for all periods of interruptive military service in their careers that were not already restored by repaying contributions– even those periods that were prior to the effective date of the bill. This option corresponds to last year's SCPP bill.

The SCPP's 2008 bill did not provide for refunds. A concern with this approach has been that persons who already paid for their interruptive military service credit may feel that they are being unfairly treated.

Option 3 – Past and Prospective Service with Refunds for Recent Service

This option seeks to provide the same free service as in Option 2, but would also pay refunds to those who already reinstated service credit for the following periods of war: Operation Iraqi Freedom (Persian Gulf) and/or Operation Enduring Freedom (southern or central Asia, including Afghanistan).

Refunding member contributions creates administrative burdens and increases cost. On the other hand, this approach may provide consistent benefits for all members participating in ongoing periods of war.

Option 4 – Past and Prospective Service with Refunds for All Service

This option would provide the same free service as in Option 2, but would also pay refunds to those who already reinstated service credit for any period of war during their career. Even more refunds would be paid from plan funds than under Option 3. This option would be the most generous to members, the most costly and the hardest to administer.

Committee Activity

The SCPP had a work session on this issue at its September meeting. The Executive Committee directed staff to bring back preliminary pricing on Options 3 and 4. Staff also updated the pricing for Option 2, which is the same as last year's SCPP-sponsored bill.

Stakeholder Input

Copies of 2008 correspondence from LEOFF 2 are attached.

Next Steps

The SCPP will decide whether to recommend legislation for one of the options presented. If so, staff will prepare draft legislation and a draft fiscal note for a public hearing.

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RCW 41.04.005
"Veteran" defined for certain purposes.

(1) As used in RCW 41.04.005, 41.16.220, 41.20.050, 41.40.170, and *28B.15.380 "veteran" includes every person, who at the time he or she seeks the benefits of RCW 41.04.005, 41.16.220, 41.20.050, 41.40.170, or *28B.15.380 has received an honorable discharge, is actively serving honorably, or received a discharge for physical reasons with an honorable record and who meets at least one of the following criteria:

(a) The person has served between World War I and World War II or during any period of war, as defined in subsection (2) of this section, as either:

(i) A member in any branch of the armed forces of the United States;

(ii) A member of the women's air forces service pilots;

(iii) A U.S. documented merchant mariner with service aboard an oceangoing vessel operated by the war shipping administration, the office of defense transportation, or their agents, from December 7, 1941, through December 31, 1946; or

(iv) A civil service crewmember with service aboard a U.S. army transport service or U.S. naval transportation service vessel in oceangoing service from December 7, 1941, through December 31, 1946; or

(b) The person has received the armed forces expeditionary medal, or marine corps and navy expeditionary medal, for opposed action on foreign soil, for service:

(i) In any branch of the armed forces of the United States; or

(ii) As a member of the women's air forces service pilots.

(2) A "period of war" includes:

(a) World War I;

(b) World War II;

(c) The Korean conflict;

(d) The Vietnam era, which means:

(i) The period beginning on February 28, 1961, and ending on May 7, 1975, in the case of a veteran who served in the Republic of Vietnam during that period;

(ii) The period beginning August 5, 1964, and ending on May 7, 1975;

(e) The Persian Gulf War, which was the period beginning August 2, 1990, and ending on the date prescribed by presidential proclamation or law;

(f) The period beginning on the date of any future declaration of war by the congress and ending on the date prescribed by presidential proclamation or concurrent resolution of the congress; and

(g) The following armed conflicts, if the participant was awarded the respective campaign badge or medal: The crisis in Lebanon; the invasion of Grenada; Panama, Operation Just Cause; Somalia, Operation Restore Hope; Haiti, Operation Uphold Democracy; Bosnia, Operation Joint Endeavor; Operation Noble Eagle; southern or central Asia, Operation Enduring Freedom; and Persian Gulf, Operation Iraqi Freedom.

[2005 c 255 § 1; 2005 c 247 § 1. Prior: 2002 c 292 § 1; 2002 c 27 § 1; 1999 c 65 § 1; 1996 c 300 § 1; 1991 c 240 § 1; 1984 c 36 § 1; 1983 c 230 § 1; 1982 1st ex.s. c 37 § 20; 1969 ex.s. c 269 § 1.]

Notes:

Reviser's note: *(1) RCW 28B.15.380 was amended by 2005 c 249 § 2 and no longer applies to veterans. For later enactment, see RCW 28B.15.621.

(2) This section was amended by 2005 c 247 § 1 and by 2005 c 255 § 1, each without reference to the other. Both amendments are incorporated in the publication of this section under RCW 1.12.025(2). For rule of construction, see

RCW 1.12.025(1).

Severability -- 2005 c 247: "If any provision of this act or its application to any person or circumstance is held invalid, the remainder of the act or the application of the provision to other persons or circumstances is not affected." [2005 c 247 § 3.]

Effective date -- 2005 c 247: "This act is necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and takes effect immediately [May 3, 2005]." [2005 c 247 § 4.]

Effective date -- 1983 c 230: "This act is necessary for the immediate preservation of the public peace, health, and safety, the support of the state government and its existing public institutions, and shall take effect July 1, 1983." [1983 c 230 § 3.]

Effective date -- Severability -- 1982 1st ex.s. c 37: See notes following RCW 28B.15.012.

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STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD
P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

May 12, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

On behalf of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Retirement Board (Board), I would like to thank you for the cooperative working relationship we have shared in the past and look forward to a similar partnership in the future.

I would like to bring several topics back to your attention as you begin preparation for the 2008 interim. It is our hope that the Select Committee on Pension Policy (SCPP) and the Board can work cooperatively on these issues to once again develop legislation. I have provided a brief summary of each topic for your reference:

Interruptive Military Service Credit

Working cooperatively last interim, the Board and the SCPP jointly endorsed a bill that would have eliminated a member's obligation to pay for interruptive military service credit if the member served during a period of war. The Board is once again interested in working cooperatively with the SCPP on the issue and feels the following additional question will need to be further explored:

- Should the benefit apply to all periods of interruptive military service which have not yet been recovered?

Inflationary Adjustment for $150,000 Death Benefit

The Board is interested in once again working with the SCPP to further study the effect of adding an inflationary adjustment to all the state retirement plans that provide the $150,000 death benefit. In addition to last year's study the Board feels following issues will need to be explored further:

- Should an adjustment in the lump sum amount be made to account for inflation since the creation of the benefit?

- Should both the lump sum adjustment and the addition of the inflationary adjustment be included in the bill?

Military Service Death Benefit

The Board and the SCPP jointly recommended legislation to the 2008 Legislature, which would have provided an unreduced annuity to qualifying survivors of members of all plans, who leave employment due to service in the National Guard or Reserves and die while in military service, during a period of war. The Board would like to continue our joint work to eliminate the "early retirement" actuarial reduction applied to the pensions of members who die while honorably serving our country.

Fish and Wildlife Enforcement Officer Service Credit Transfer

The Board and the SCPP also jointly recommended legislation last session that would have permitted Department of Fish and Wildlife Enforcement Officers to transfer service credit earned in the Public Employees' Retirement System (PERS) Plan 2 as enforcement officers into the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2. The Board feels the following issue may need to be further explored as well:

- Should PERS 3 members be included in the transfer group?

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

We would be happy to meet with you to discuss these topics at an upcoming SCPP or LEOFF Plan 2 Retirement Board meeting. Thank you for your consideration and we look forward to working with you.

Sincerely,

Kelly L Fox

Kelly Fox, Chair

cc: Matt Smith, State Actuary

STATE OF WASHINGTON
LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD
P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

June 30, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

At the recent meeting of the Select Committee on Pension Policy (SCPP) the chairman requested that the Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board (LEOFF 2 Board) provide a prioritized list of the suggested joint topics that the LEOFF 2 Board would like to work on cooperatively with the SCPP.

During the course of the most recent LEOFF 2 Board meeting we prioritized the suggested topics for cooperation in the following order:

1. **Fish and Wildlife Enforcement Officer Service Credit Transfer**
   Allow FWEO members to transfer their PERS Plan 2 service as enforcement officers to LEOFF Plan 2.

2. **Inflationary Adjustment for $150,000 Death Benefit**
   The $150,000 lump-sum death benefit paid to survivors of public employees who die in the line of duty is not adjusted for inflation.

3. **Interruptive Military Service Credit**
   Members whose public employment is interrupted by military service are required to pay member contributions in order to purchase service credit.

4. **Military Service Death Benefit**
   Beneficiaries of members who die while serving on active duty with the United States Military do not qualify for duty related death benefits.

5. **Purchase of Annuity**
   Members are limited in the amount of money they can convert to a defined benefit by the amount required to purchase 5 years of service.

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

Thank you for your consideration and we look forward to working with you.

Sincerely,

Kelly L Fox

Kelly Fox, Chair

cc: Matt Smith, State Actuary

The Select Committee on Pension Policy

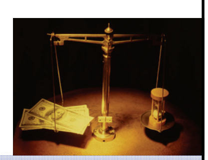
Interruptive Military Service Credit

Laura Harper, Policy and Research Services Manager
November 18, 2008

Office of the State Actuary
"Securing tomorrow's pensions today."

The Issue Today…

- Whether to grant free interruptive military service credit to those who serve during a period of war
- Follow-up from SCPP work session in September
  - Staff directed to bring back preliminary pricing for options
- Today's briefing
  - Recap of policy decisions made in past
  - Review of options and pricing



SCPP Proposed A Bill In 2008

- Interruptive military service credit would be free to those serving in a period of war
  - Members relieved from repaying member contributions
  - Employers still pay employer contributions plus interest
- "Period of war" is already defined in state statute
  - Declared wars
  - Armed conflicts

Who Did The 2008 Proposal Affect?

- Members of the open plans
  - Plans 2 and 3 of PERS, TRS, and SERS
  - LEOFF 2
  - PSERS
  - Washington State Patrol Plan 2
- Anyone eligible to apply after the bill's effective date
  - Members must apply before retiring
  - The service credit could have been earned any time in the member's career

2008 Proposal Did Not Pass

- LEOFF 2 Board asked SCPP to look more closely at how the benefit is applied
  - Complaints that members who already reinstated service credit were, in effect, penalized
  - Inconsistent treatment for members who served in same conflicts
- SCPP looked at several new options

Options For Applying The Benefit

- Option 1: Future service
- Option 2: Past and future service, no refunds
- Option 3: Past and future service, refunds for service in ongoing conflicts
  - Operation Iraqi Freedom - began 3/4/03
  - Operation Enduring Freedom (including Afghanistan) – began 10/7/01
- Option 4: Past and future service, refunds for all service

Preliminary Fiscal Costs

($ in millions)	**Option 2 Past & Future No Refunds**	**Option 3 Past & Future Refunds for Recent Service**	**Option 4 Past & Future Refunds for All Service**
2009-2011			
Total GFS	$0.0	$0.0	$0.0
Total Employer	0.0	0.0	0.0
25-Year			
Total GFS	0.7	1.1	1.1
Total Employer	$2.5	$3.8	$4.0

Next Steps

- Recommend an option
  - Direct staff to bring back a bill draft and draft fiscal note
  - Schedule a public hearing
- Take no action

6. Plan 1 COLA Proposals

Plan 1 COLA Proposals

Description of Issue

The SCPP is being asked to revisit the Uniform COLA in PERS and TRS Plan 1. Stakeholders seeking improvements to the COLA have proposed two possible changes. This issue raises three basic policy questions:

- ❖ Is the current COLA sufficient?
- ❖ Who most needs an improved COLA?
- ❖ What form should a new COLA take?

Policy Highlights

- ❖ The Uniform COLA helps maintain the value of pensions—though not equally for all members.
- ❖ The Uniform COLA and the Plans 2/3 COLA were designed to meet different policy objectives—direct comparisons may be misleading.
- ❖ The SCPP has adopted policy on inflation protection.
- ❖ Benefit improvements for past service increase the Plans 1 UAAL and generally run counter to the principle of intergenerational equity.
- ❖ There are a variety of ways to target, implement, and design COLAs.

Committee Activity

Staff briefed the full SCPP on this issue in September. At the Executive Committee meeting that followed, the stakeholders requested the Committee allow them to revise the proposals under consideration. A work session on the revised proposals was scheduled for November.

Revised Stakeholder Proposals:

- **Short-Term: Grant additional increases to the Uniform COLA based on year of retirement.**
  - Provides larger increases to members retired the longest.
  - Does not precisely recover purchasing power.
  - Impacts minimum benefits.
- **Long-Term: Provide the better of the Uniform COLA or a CPI-based COLA similar to the Plans 2/3 COLA.**
  - Generally prevents the further loss of purchasing power.
  - Does not diminish benefits.
  - Provides similar value for the CPI-based COLA, but a better overall COLA in the Plans 1 than the Plans 2/3.
  - Raises questions about contractual rights.

What is the Next Step?

The Committee will decide whether or not to revisit this issue. Options include:

- Take no further action.
- Direct staff to draft legislation based on one or more of the stakeholder proposals.
- Study additional options.

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Plan 1 COLA Proposals

In Brief

ISSUE

The SCPP is being asked to revisit the COLA provided in the PERS and TRS Plans 1. Stakeholders seeking improvements to the COLA have proposed two possible changes (see page 17). The first modifies the design of the existing COLA by granting additional increases based on the year of retirement. The second provides the better of the existing service-based COLA or a new CPI-based COLA.

MEMBER IMPACT

These proposals would affect very different member groups. The first would impact nearly 33,000 PERS and TRS Plan 1 members retired prior to 1991. The second would impact over 114,000* PERS and TRS Plan 1 active, terminated vested, and retired plan members.*

**As of June 30, 2007.*

Darren Painter
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Introduction

The SCPP is being asked to revisit the post-retirement Cost-Of-Living-Adjustment (COLA) provided in Plan 1 of the Public Employees' Retirement System (PERS) and the Teachers' Retirement System (TRS). (The term "Plans 1" will be used throughout to refer to PERS and TRS Plan 1.) This issue raises three basic policy questions:

- Is the current COLA sufficient?
- Who most needs an improved COLA?
- What form should a new COLA take?

This paper will explore the policy considerations around these questions and the challenges faced by policy makers when trying to retrofit a COLA into a plan that was not originally designed for one.

Stakeholders have revised their proposals since the September meeting. Discussion of the revised proposals begins on page 17.

Current Situation

The primary COLA provided in the Plans 1 is the Uniform COLA. The Uniform COLA is a service-based COLA payable the first calendar year in which the recipient turns age 66 and has been retired for one year. The Uniform COLA is a fixed-dollar amount multiplied by the member's total years of service. The dollar amount of the Uniform COLA increases by 3 percent every year on July 1. As of July 1, 2008, the Uniform COLA was $1.73 per month/per year of service. This amounts to an annual increase of $623 for a recipient with 30 years of service. Statute specifies that future increases to the Uniform COLA are not a contractual right.

An optional Consumer Price Index (CPI)-based automatic COLA is also available to the Plans 1 members who elect it at retirement. The Auto-COLA* provides an annual percentage increase in the retirement allowance. The increase is based on changes in the CPI** up to a maximum of 3 percent per year (essentially the same COLA as provided in the Plans 2/3). The Auto-COLA begins one year after retirement—regardless of age or service—and is in addition to any other COLAs received. Members who elect the Auto-COLA receive an actuarially reduced retirement allowance to offset the cost.

COLAs address how well a pension maintains its value, while minimum benefits address the adequacy of a pension.

The Plans 1 also provide minimum retirement benefits in addition to the COLAs discussed above. While COLAs address how well a pension maintains its value over time, minimum benefits address the adequacy of a pension and serve as a safety net. Minimum benefits increase every year—effectively providing a COLA to those at the minimum benefit level. Two minimums are provided: the Basic and the Alternative.

The Basic Minimum is $38.92*** per month multiplied by the member's total years of service. The Alternate Minimum is $1,092.73*** a month for recipients who:

a) Have at least 25 years of service and have been retired at least 20 years.

b) Have at least 20 years of service and have been retired at least 25 years.

The Basic Minimum increases every year by the dollar amount of the Uniform COLA. (For example, the Basic Minimum increased from $37.19 to $38.92 in 2008. The $1.73 increase was the amount of the Uniform COLA for that year.) The Alternate Minimum is not tied to the Uniform COLA and increases by 3 percent each year.

**First available in 1990.*
***Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) for Seattle-Tacoma-Bremerton (STB).*
****As of July 1, 2008.*

Example

Figure 1 illustrates the impact of the Uniform COLA on three retirees with 30 years of service and different monthly pensions. In this example, Retiree 3 receives the Basic Minimum benefit—which increases by the Uniform COLA amount each year.

Figure 1

Uniform COLA Example: 30 Years of Service				
	Pension Before COLA	2008 Uniform COLA ($1.73*30)=51.90	Pension After COLA	Percent Increase
Retiree 1	$1,500.00	$51.90	$1,551.90	3.46%
Retiree 2	$3,000.00	$51.90	$3,051.90	1.73%
Retiree 3	$1,115.70 (Basic Minimum)	$51.90	$1,167.60 (Basic Minimum)	4.65%

The Uniform COLA provides proportionately higher increases for annuitants with smaller pensions.

This example shows how the Uniform COLA provides proportionately higher increases (and greater purchasing power protection) for annuitants with smaller pensions. This is because the Uniform COLA is a fixed dollar amount and not based on a percentage of the pension.

History

To understand where today's COLA policy came from, it is helpful to look at the history of COLA policy from different perspectives. The broader perspective is how COLA policy has changed within the context of plan design. A more narrow focus is how the Legislature has addressed COLAs within the Plans 1.

COLA Policy has Changed over Time

When the Plans 1 were first created over 60 years ago, they did not provide for post-retirement COLAs. COLAs may not have been provided for a variety of reasons:

The Plans 1 were not originally designed to provide a COLA.

- ❖ Inflation was relatively low from 1940 until the early 1970s.
- ❖ Members were not expected to live many years in retirement.
- ❖ The plans were intended to provide more of a reward for service than replacement income.

Eventually, changing times began to challenge this design. Periods of high inflation, increasing life spans, and increasing expectations for retirement all called into question the adequacy of the Plans 1 design. These challenges led to a rethinking of the basic purpose of retirement plans.

The Plans 2 were designed from the onset to provide a COLA.

Responding to challenges with the Plans 1 design, the Plans 2 were created in 1977. The Plans 2 were designed from the onset to be income replacement plans and to provide a post-retirement COLA. Part of this design was the establishment of a normal retirement age of 65—substantially higher than the retirement ages in Plans 1. The higher retirement age made the COLA more affordable and increased the likelihood the COLA would reasonably protect the value of the pension over the recipient's life.

The Plans 2 income replacement and COLA policy was carried forward into the design of the Plans 3 when those plans were created in the late1990s.

Benefits for Plans 1 Retirees have Increased over Time

COLA policy also changed within the Plan 1 design to a more limited extent. Responding to concerns about the adequacy of benefits and the impact of inflation, policy makers made several efforts over the years to increase benefits for retirees in the Plans 1. These efforts continued even after they closed.

The Legislature has employed a variety of different approaches in their efforts to increase retiree benefits:

Various approaches have been used to increase retiree benefits.

- ❖ Establishing minimum benefits and periodically increasing them to reflect changes in the cost-of-living.
- ❖ Granting various ad-hoc benefit increases.
- ❖ Granting increases based on earnings realized by plan assets.
- ❖ Providing an optional, CPI-based COLA from retirement paid for by members.
- ❖ Providing automatic COLAs (including Uniform).

Appendix A provides a history of post-retirement benefit increases in the Plans 1. Some highlights from this history are provided in **Figure 2,** below.

Figure 2

Key Post-Retirement Benefit Adjustments in The Plans 1	
Year	**Increase**
1961	Minimum benefit established.
1970-1986	Various ad-hoc COLAs (3% - 6%) and Minimum benefit increases.
1987	3% automatic annual increase in Minimum benefit.
1989	CPI-based automatic COLA (up to 3%) for retirees whose purchasing power at age 65 drops more than 40%.
1995	Uniform COLA replaces CPI-based COLA.
1998	Gain-sharing established. Provided possible even-year increases in the Uniform COLA depending on investment earnings.
2008	Gain-sharing ended. Replaced by one-time increase to Uniform COLA.

SCPP Action Taken on Plans 1 COLA Policy

The SCPP has made several recommendations on COLAs in the Plans 1.

The SCPP studied the issue of purchasing power for Plans 1 retirees in 2003 and 2004, and received an update on the issue in 2005.

The SCPP has made several recommendations on COLAs in the Plans 1 that have been adopted by the Legislature.

2003*

- $1,000 Alternative Minimum benefit for members with 25+ years of service and retired 20+ years.

2004*

- $1,000 Alternative Minimum benefit for members with 20+ years of service and retired 25+ years.
- Increase the amount of the Alternative Minimum by 3 percent each year.
- One-time increase in the Uniform COLA.
- Provide the Uniform COLA to members who will turn age 66 during the calendar year.

Indicates year first recommended. Some proposals were recommended in more than one year. See **Appendix A for year enacted.*

Policy Analysis

Other Washington Plans

The Plans 2/3 provide a CPI-based COLA.

Washington's Plans 2/3 provide a CPI-based COLA. This COLA is designed to maintain the purchasing power of retiree benefits and is consistent with the underlying income replacement design of the plan. The Plans 2/3 COLA is an annual percentage increase in the retirement allowance beginning one year after retirement. The increase is based on changes in the CPI* up to a maximum of 3 percent per year.

As discussed in the **History** section, the Plans 2/3 COLA is tied to a normal retirement age of 65 (or 62 with 30 years of service). Members who retire prior to the normal retirement age still receive the COLA after one year—but on an actuarially reduced benefit.

**Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) for Seattle-Tacoma-Bremerton (STB).*

Peer Systems

Washington's peer systems provide automatic CPI-based or fixed-percent COLAs.

All of Washington's peer systems provide an automatic post-retirement COLA in their open plans (see **Figure 3**). Five of those systems provide COLAs that are CPI-based with varying caps from 2 to 6 percent. The remaining systems provide fixed percent increases ranging from 1.5 to 3.0 percent. Systems where members are not covered by Social Security tend to provide larger COLAs. Most COLAs begin after one year of retirement; Florida and Idaho provide prorated COLAs for those retired less than one year.

Several of the peer systems provide protection against specific losses of purchasing power. Benefits in the California systems cannot fall below a minimum percent (75 or 80 percent) of the original benefit's purchasing power. Benefits in the Seattle system cannot fall below 60 percent of their original purchasing power. This is similar to a 1992 COLA provision that protected Plans 1 members from the loss of more than 40 percent of their age 65 benefits' purchasing power.

Figure 3

COLA Provisions by Select Retirement Systems*	
System	**COLA**
Cal PERS	CPI based, 2% max (75% purchasing power min.)
Cal STRS	2% simple (80% purchasing power min.)
Colorado PERA**	CPI up to 3%
Florida (FRS)	3%
Idaho (PERSI)	CPI based, 1% min, 6% max,
Iowa (IPERS)	Simple, 3% max, tied to investment surplus
Minnesota (MSRS)	CPI based, 2.5% max + investment surplus
Missouri (MOSERS)**	80% of change in the CPI, 5% max
Ohio (OPERS)**	CPI based, 3% max
Oregon PERS**	CPI based, 2% max
Seattle (SCERS)	1.5% (60% purchasing power min.)

*For new hires. Source: Member handbooks published on system administrators' websites as of 8/28/2008.

**Not covered by Social Security.

Some state plans only provide ad-hoc COLAs.

While all of Washington's peer systems provide automatic CPI-based or fixed-percent COLAs, some states do not. According to the 2007 Public Fund Survey (a national survey of 126 retirement plans representing all 50 states), 26 state plans provide COLAs only on an ad-hoc basis. Also, 15 state plans provide COLAs that are in some part based on investment earnings. The remaining plans (nearly two-thirds) generally provide automatic CPI-based or fixed-percent COLAS.

Providing Adequate Benefits and Protecting Purchasing Power are Different Policy Objectives

COLA policy has largely been driven by adequacy of benefits and purchasing power concerns.

COLA policy in the Plans 1 has largely been driven by the twin concerns of adequacy of benefits and purchasing power protection. Though there is some overlap, the two are very distinct concepts from a plan-design perspective and have different policy implications.

Adequacy of benefits relates to how well a pension *meets expectations* around a standard of living. In contrast, purchasing power protection relates to how well a pension *retains value* over time. To illustrate the difference: the pension of a highly-paid retiree might lose considerable value over time and still be considered "adequate," while the pension of a low-paid retiree might retain its full value over time but be considered "inadequate."

Purchasing power protection is addressed through COLAs.

Adequacy of benefits may be addressed through a variety of means including changing benefit formulas or establishing minimum benefits. Purchasing power protection is addressed through COLAs. The remainder of this paper will focus on policies around purchasing power protection.

The Uniform COLA and Plans 2/3 COLA were Designed to Meet Different Objectives

Discussions of COLA policy in the Plans 1 often involve comparisons between the Uniform and the Plans 2/3 COLA. These COLAs were designed to meet different policy objectives. Direct comparisons between them can be misleading.

The Uniform COLA is designed to meet four primary policy objectives within fiscal constraints:

The Uniform COLA provides more purchasing power protection to members with lower salaries.

- ❖ Provide a larger dollar increase to members with more service.
- ❖ Provide more purchasing power protection to members who retire with lower salaries.
- ❖ Provide a COLA at the same age that Plans 2/3 members qualify for an unreduced COLA.
- ❖ Provide legislators a simple mechanism to grant ad-hoc COLAs.

These objectives are consistent with the reward-for-service design of the Plans 1 and reflect trade-offs between adequacy of benefits and purchasing power protection. Tying the Uniform COLA to the Plans 2/3 unreduced retirement age may reflect a desire to maintain consistency between the plans in the starting age for unreduced COLAs. The design of the Uniform COLA also provides a simple mechanism for legislators to grant ad-hoc COLAs—the most recent example being the 40 cent (per month/per year of service) increase granted in 2008.

In contrast to the Uniform COLA, the Plans 2/3 COLA is designed to maintain the value of members' pensions in an environment of moderate inflation. The Plans 2/3 COLA

The Plans 2/3 COLA is designed to maintain purchasing power for all retirees.

does not favor any one group of retirees. Retirees with relatively high salaries and high benefits receive the same protection from inflation as lower-salary, lower-benefit retirees. This is consistent with the underlying income-replacement design of the plan.

The Uniform and the Plans 2/3 COLA both provide inflation protection consistent with their respective plan designs. While the Plans 2/3 COLA generally does a better job of maintaining the value of the pension than the Uniform COLA, there are exceptions. Some Plans 1 retirees may receive proportionately larger increases under the Uniform COLA than they would under the Plans 2/3 COLA. These would tend to be recipients of minimum benefits or low-wage, high-service retirees.

Existing Policies Impact this Issue

There are three key policies that are relevant to a discussion of this issue:

- ❖ Inflation protection.
- ❖ Intergenerational equity.
- ❖ Amortization of Plan 1 unfunded liabilities.

The SCPP adopted a policy goal directly related to inflation protection.

The SCPP adopted a policy goal directly related to inflation protection. The goal is: "to increase and maintain the purchasing power of retiree benefits in the Plans 1 of PERS and TRS, to the extent feasible, while providing long-term benefit security to retirees." The Legislature has taken actions that support this goal by providing various automatic COLAs not included in the original design of the Plans 1. This includes the Uniform COLA and automatic increases in minimum benefits.

A desire that retiree benefits should have some form and degree of protection from inflation is also evident in the creation of the Plans 2/3. These plans included a CPI-based automatic COLA in the original plan design.

Intergenerational equity requires benefits to be funded over the working lifetime of the member.

Another policy that impacts this issue is the Legislature's funding policy based on the concept of intergenerational equity. The policy is to fund, to the extent feasible, benefit increases for Plans 1 members over the working lives of those members so that the cost of those benefits are paid by the taxpayers who receive the benefit of those members' service [RCW 41.45.010 (4)].

Benefit increases granted to retired members are inconsistent with the concept of intergenerational equity. Why? None of the cost can be funded over their working lifetimes since they are already retired. Instead, the cost is generally born by taxpayers who never received services from the members.

Providing benefit improvements for active Plans 1 members consistent with intergenerational equity presents policy makers a challenge as well. Active members in the Plans 1 are generally close to retirement. This leaves limited opportunity to fund the cost of improved benefits over the remainder of their working lifetimes. Therefore, the source of contributions to fund benefit improvements increasingly becomes taxpayers who never received services from these members.

The cost of Plans 1 benefit improvements not funded over the members' working lifetimes is passed along to Plans 2/3 employers. All Plans 2/3 employers are required to make additional contributions to pay for these Plans 1 benefits.

Benefit improvements for past service increase the Plans 1 UAAL.

Benefit improvements for past service increase the Unfunded Actuarial Accrued Liability (UAAL) for the Plans 1. The UAAL exists because benefits already earned by Plans 1 members have not been fully paid for. Current funding policy requires that the UAAL in the Plans 1 be fully paid by June 30, 2024 [RCW 41.45.010(2)]. The level of benefit improvements that can be financed over the remaining amortization period may serve to constrain policy options.

COLA Policy may Impact Human Resource Policies

COLA policy in the Plans 1 may have an impact on human resource policies around post-retirement employment and retention.

The lack of a COLA for Plans 1 members prior to age 66 may encourage post-retirement employment. Returning to work after retirement may seem an attractive option for those who wish to accumulate additional assets to offset future inflation and other post-retirement expenses. This may lead to greater pressure for expanded post-retirement employment opportunities. In 2001, the Legislature expanded the post-retirement employment program for the Plans 1. The expansion allows Plans 1 retirees to work significantly more hours than Plans 2/3 retirees without having their pensions suspended.

On the flip side, providing a COLA in the Plans 1 prior to age 66 may encourage more Plans 1 members to retire at earlier ages. Such an outcome may conflict with employers' desire to retain their most experienced workers.

Several Factors may Impact Purchasing Power.

Policy makers seeking to answer questions about the need for an improved COLA in the Plans 1 may also turn to an economic approach. An economic approach to COLA policy considers the impact of inflation on the purchasing power of retiree pensions. When balanced with the overall policy considerations, an economic analysis may provide additional focus for further policy discussion.

Purchasing power is a measure of how well a pension retains its value over time.

Purchasing power is a measure of how well a pension retains its value over time. Purchasing power is measured by comparing the change in the member's pension over time with the amount of inflation over the same time period. Purchasing power is impacted by three factors:

- Inflation after retirement.
- Length of retirement.
- Post-retirement COLAs.

Inflation is the driving force behind the decline in the relative value of a pension over time. Members who retire during periods of high inflation will generally lose more purchasing power than members who retire during periods of relatively low inflation. See **Appendix B** for a history of inflation.

Likewise, members who are retired for a longer period of time are likely to lose more purchasing power due to post-retirement inflation than members who are retired for shorter periods. Earlier retirement ages and increasing life spans are significant factors in the loss of purchasing power experienced by some members.

Post-retirement COLAs help maintain purchasing power.

Post-retirement COLAs offset the effects of inflation and help maintain purchasing power. The Legislature has provided numerous COLAs in the Plans 1 (see **Appendix A**). Members who receive less in COLAs will generally lose more purchasing power over time than members who receive more in COLAs.

Figures 4 and 5 show the purchasing power for PERS and TRS Plans 1 service retirees by year of retirement. The Original Benefit line shows the purchasing power had no COLAs been provided. The Current Benefit line shows the purchasing power after factoring in all COLAs. The differences in purchasing power between the systems reflect the impact of COLAs received.

Figure 4
Purchasing Power of PERS 1
Service Benefits in 2008

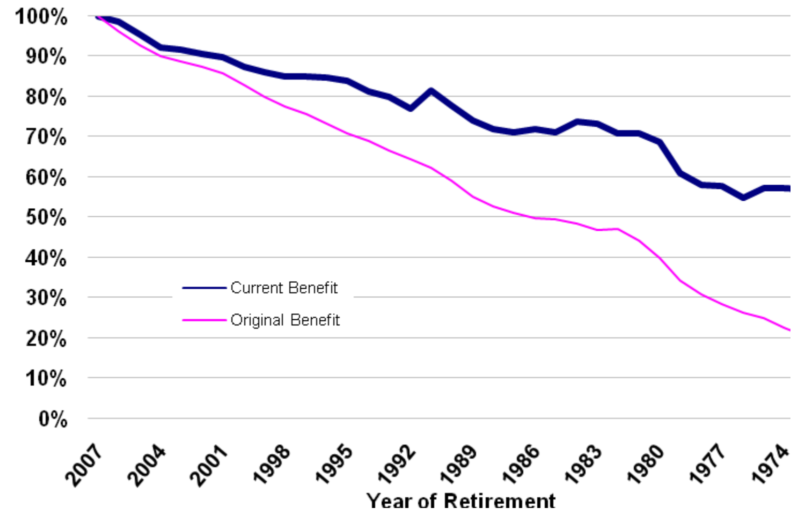
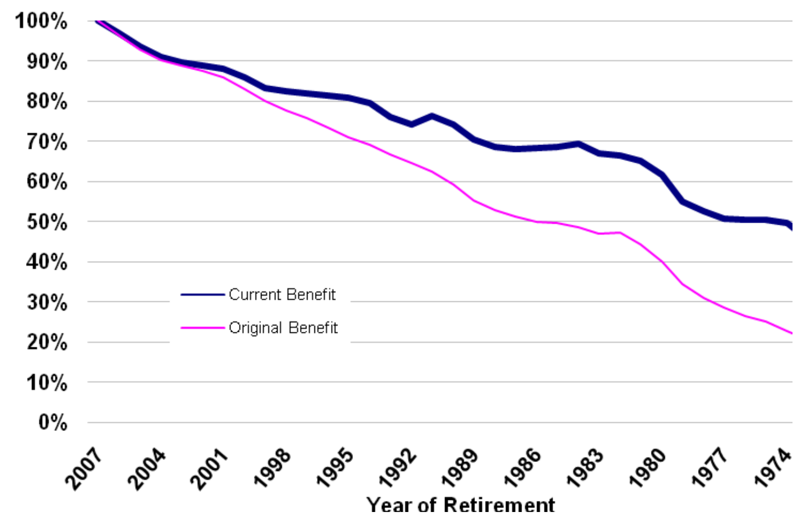


Figure 5
Purchasing Power of TRS 1
Service Benefits in 2008



Purchasing power for Plans 1 members who retired at the same time may vary widely from the group average due to post-retirement increases. The Plans 1 have provided numerous post-retirement benefit increases that were not designed to uniformly recover purchasing power. These include increases to minimum benefits, certain ad-hoc COLAs, and Uniform COLA increases. These increases impact members within the same group differently. Generally, the increases have served to recover more purchasing power for retirees with lower pensions.

The Uniform COLA Helps Maintain the Value of Pensions

Some Uniform COLA recipients will continue to lose purchasing power.

A closer look at how the current Uniform COLA impacts purchasing power is relevant to a discussion of purchasing power within the Plans 1. The Uniform COLA helps maintain the value of a recipient's pension from age 65. Because the Uniform COLA is a dollar amount per year of service, it provides the greatest inflation protection for members who retired with the smallest salaries (This includes members who worked lower-paying jobs, and members who retired many years ago when wages were generally lower.) Members who retire prior to age 65 may lose a significant amount of purchasing power in their pension before they receive their first Uniform COLA increase. Once they receive the Uniform COLA, the impact on purchasing power will vary. Some recipients (lower-salaried) may maintain or even recover lost purchasing power during some years, while others (higher-salaried) will face a continued erosion of purchasing power.

COLA Policy is a Balance

COLA policy reflects a balance between various concerns.

As discussed earlier in this paper, current COLA policy in the Plans 1 reflects a balance between various concerns:

- Inflation protection.
- Adequacy of benefits.
- Intergenerational equity.
- Funding.
- Human resources.

Policy makers may wish to consider whether or not the current balance is appropriate when evaluating the sufficiency of the Plans 1 COLA.

Key Questions in Shaping New COLA Policy

The first part of this paper has explored the question of whether or not the current COLA in the Plans 1 is sufficient. If policy makers feel the COLA needs improvement, they may next consider who most needs an improved COLA and what form the COLA should take. Answers to these key questions will help shape any new COLA policy.

COLAs can be Targeted

COLAs may be directed to individuals with the greatest perceived need.

It is likely that substantial improvements to the Plans 1 COLA will face fiscal constraints. Policy makers may then choose to direct limited COLA dollars to those individuals who they perceive as having the greatest need for a COLA. COLAs can be targeted to recipients based on loss of purchasing power, years retired, years of service, or size of benefit. If policy makers desire to maintain purchasing power they will likely target COLAs based on purchasing power or years retired. If the desire is to reward long careers, then COLAs will likely be targeted to members with many years of service. If the concern is adequacy of benefits, then COLAs will likely be targeted to members with the lowest pensions.

Besides directing dollars to recipients with the most need, targeting COLAs may serve other policy needs such as controlling costs or maintaining equity across the plans.

COLAs may be Implemented Many Different Ways

COLAs may be ad-hoc or automatic.

The form that an improved COLA takes depends on the goals of policy makers. COLAs may be implemented in a variety of ways to achieve specific policy objectives. COLAs may be implemented on a one-time or ongoing basis, and the payment may take many forms.

Ad-hoc COLAs are one-time increases given to retirees. Ad-hoc COLAs can be very effective at making up for past inflation, but usually do little to address future inflation. Ad-hoc COLAs can give policy makers the most flexibility in reacting to specific situations and in controlling costs. When COLAs are ad-hoc, there is often little or no pre-funding—effectively making them pay-as-you-go benefit improvements.

In contrast, automatic COLAs are ongoing increases and usually benefit both active and retired members. Automatic COLAs can be very effective at protecting benefits against future inflation, but may do little to address lost purchasing power due to past inflation. Automatic COLAs may be preferred from the member viewpoint since they are ongoing and don't require continual action by policy makers. However, for the same reasons, it may be more difficult to fine-tune an automatic COLA for a specific situation. Because automatic COLAs are ongoing and more forward-looking, they offer greater opportunities for pre-funding. Pre-funding reduces the contributions required for a benefit improvement since more of the cost of the improvement is paid for by future investment returns.

COLA payments may take many forms. Some of these include:

COLA payments may take many forms.

- ❖ Percentage based on a CPI.
- ❖ Fixed percentage.
- ❖ Flat dollar amount.
- ❖ Dollar amount per year of service.

CPI-based COLAs are the most direct way to protect a benefit against inflation since the COLA is based on actual, measured inflation. CPI-based COLAs provide the same inflation protection to all recipients regardless of the size of their pension. CPI-based COLAs often have an annual cap to control costs. However, an annual cap means that recipients will lose purchasing power when inflation exceeds the cap.

Fixed-percentage COLAs (i.e., 2 or 3 percent) protect against a set amount of inflation while controlling costs. They provide the same amount of inflation protection to all recipients regardless of the size of their pension. However, recipients will lose purchasing power when inflation exceeds the fixed percent.

Flat-dollar-amount COLAs (i.e., $100/month) provide proportionally greater increases to recipients with smaller pensions. While they may do little to protect purchasing power for retirees with larger pensions, flat-dollar-amount COLAs are an effective way to address adequacy of benefit concerns.

Dollar-amount-per-year-of-service COLAs (i.e., $10/month/year of service) provide larger increases to members with more service and proportionally larger increases to members who retired with lower salaries. This type of COLA is a blend between adequacy of benefits and reward for service policies. It may do little to protect the purchasing power of high-salaried retirees. The Uniform COLA is an example of this type of COLA in the Plans 1.

COLAs might be impacted by IRS requirements.

Any of the COLA designs mentioned above might be impacted by Internal Revenue Service (IRS) requirements. Some designs might result in COLAs that do not conform to IRS requirements for tax-qualified plans or must be administratively reduced to comply with IRS requirements. This is more likely to be an issue with COLAs designed to make up for long periods of past inflation. Policy makers may wish to consult tax counsel before making significant changes in COLA policy.

Policy Makers have Flexibility in Crafting COLA Policy

Policy makers have a great deal of flexibility in crafting new COLA policy for the Plans 1. Policy makers may target, implement, and design COLAs in a variety of ways to support their policy objectives. Any new COLA policy may be constrained by fiscal and IRS considerations.

Conclusion

The issue of COLAs in the Plans 1 raises three basic questions for policy makers.

- Is the current COLA sufficient?
- Who most needs an improved COLA?
- What form should a new COLA take?

In considering these questions, policy makers will likely balance a wide variety of concerns including inflation protection, adequacy of benefits, intergenerational equity, funding, and human resources. The current Plans 1 Uniform COLA reflects trade-offs between these various concerns.

Any change to the Uniform COLA will likely involve further trade-offs. Given likely fiscal constraints, policy makers may choose to direct limited COLA dollars to recipients with the greatest perceived need.

Revised Stakeholder Proposals

Following the September SCPP briefing on this issue, stakeholders submitted revised COLA proposals to the committee for consideration. This paper has been updated to reflect the revised proposals.

Stakeholders are seeking improvements in the COLAs provided to PERS and TRS Plan 1 retirees. The stakeholders have proposed both a short-term and a long-term option. The short-term option modifies the design of the existing Uniform COLA by granting additional increases based on the year of retirement. The long-term option provides the better of the Uniform COLA or a CPI-based COLA similar to the Plans 2/3 COLA.

Preliminary pricing of the revised short-term option will be available at the November meeting.

Proposal 1: Revised Short-Term Option

Increase the 2009 Uniform COLA by the following additional amounts based on year of retirement:

Year Retired	Increase Amount *($ per month/per year of service)*
1985-1990	$0.35
1980-1984	$0.50
1979 and earlier	$0.75

This option has several broad policy implications that are discussed in more detail below. These include:

- ❖ Modifies existing COLA policy.
- ❖ Provides larger increases to members retired the longest.
- ❖ Does not precisely replace purchasing power.
- ❖ Impacts minimum benefits.

Modifies Existing COLA Policy

This option is consistent with the reward-for-service design.

This option would establish a new policy objective within the existing Uniform COLA design. The new policy would grant different COLAs based on year of retirement. This differs from the current Uniform COLA design of granting the same increase to all members with the same service. However, it is consistent with the reward-for-service design of the Plans 1 since the COLA amount is still based on years of service—within each group. No additional increases are provided for members who retired after 1990. However, policy makers may feel less need to provide an additional COLA to these members since they had the option of purchasing the CPI-based Auto-COLA at retirement.

Provides Larger Increases to Members Retired the Longest

Some members who have been retired longer have not necessarily lost more purchasing power.

This option grants larger COLA increases to members who have been retired longer. Some members who have been retired longer have not necessarily lost more purchasing power after factoring in past COLAs. To more precisely replace lost purchasing power would require measuring purchasing power on an individual basis—which may be more complex to administer.

Does not Precisely Recover Purchasing Power

Targeting COLAs on a group basis does not precisely recover an individual's lost purchasing power. The purchasing power of individuals within the group varies due to past COLAs. This means that some members will benefit more than others in any group approach. The large differences between the steps of the increases further increase this discrepancy for some members. As an extreme example, a member who retired in 1979 will receive a COLA that is 50 percent larger than a member who retired in 1980—even though inflation was only 16.1 percent between 1979 and 1980. While this approach does not precisely recover purchasing power for an individual, it is relatively easy to administer and does provide larger increases to groups that have lost more purchasing power.

Impacts Minimum Benefits

Some may view this as effectively creating four different Basic Minimum benefits.

This proposal has implications for minimum benefit policy because the Basic Minimum is tied to the Uniform COLA amount. The proposal would result in recipients of the Basic Minimum receiving different total benefit amounts based on the year they retired. Some policy makers may view this as effectively creating four different Basic Minimum benefits based on year of retirement. Others may view this as providing an additional COLA for those who have been retired longer, on top of the Basic Minimum. However this is viewed, it raises certain policy questions.

Minimum benefits are intended to provide an adequate standard of living for recipients. Policy makers may question whether it is appropriate to effectively establish different standards of living based solely on length of retirement. For example, does someone retired for 30 years require a larger pension to maintain an adequate standard of living than someone retired for only five years? The Legislature set a precedent for providing higher minimum benefits based on years retired when it established the Alternate Minimum benefit in 2004. Policy makers exploring this option may wish to consider if the Basic Minimum should continue to be linked to the Uniform COLA or if a different increase mechanism would be preferable.

Proposal 2: Revised Long-Term Option

Provide the better of the Uniform COLA or a CPI-based COLA similar to the Plan 2/3 COLA:

- CPI from retirement up to 3 percent maximum a year.
- Starts the year the retiree turns age 66.
- Prospective only.

This option has several broad policy implications that are discussed in more detail below. These include:

- Establishes a new COLA policy.
- Generally prevents further loss of purchasing power.
- Does not diminish benefits.

- Provides a CPI-based COLA with similar value to the Plans 2/3 COLA.
- Provides a better overall COLA in the Plans 1 than in the Plans 2/3.
- Raises questions about contractual rights.

Establishes a New COLA Policy

This option is more consistent with an income replacement design.

This option would establish a new* COLA policy for the Plans 1, basing COLAs on actual inflation—regardless of service or salary. This policy is more consistent with an income replacement plan design such as the Plans 2/3. It is also a departure from the current policy to provide more inflation protection to members who retired with lower salaries.

**A CPI-based COLA was provided from 1989-1994. The COLA began after a member lost more than 40 percent of purchasing power from age 65.*

Generally Prevents the Further Loss of Purchasing Power

It will not recover lost purchasing power.

Providing this COLA on a prospective basis will generally prevent the further erosion of purchasing power for current and future retirees—as long as long-term inflation averages 3 percent or less. It will not recover purchasing power already lost due to inflation.

Does not Diminish Benefits

Providing the better of the Uniform COLA or the proposed CPI-based COLA ensures that retirement benefits are not diminished for any member. (Some would receive larger increases under the Uniform COLA; others, under the CPI-based COLA.) Policy makers may prefer to *not* diminish benefits in order to avoid raising issues around contractual rights protections.

Provides a CPI-Based COLA with Similar Value to the Plans 2/3 COLA

The proposed CPI-based COLA would start at age 66—the same age that Plans 2/3 members with less than 30 years of service* qualify for an unreduced COLA. Tying the proposed CPI-based COLA to the Plans 2/3 unreduced retirement age ensures the two COLAs generally provide similar value. This is because Plans 1 and Plans 2/3 members will generally receive the full value of a CPI-based COLA starting at the same age. Starting the proposed CPI-based COLA at age 66 is also consistent with current practice in the Uniform COLA.

**Members with 30 or more years of service qualify at age 62.*

Provides a Better Overall COLA in the Plans 1

This option provides a better overall COLA, going forward, in the Plans 1 than in the Plans 2/3. This is because Plans 1 members would receive the *better* of a COLA similar to the Plans 2/3 COLA or the Uniform COLA. In other words, the Plans 2/3 COLA becomes the new baseline COLA in Plan 1—with some members (Uniform COLA recipients) receiving additional amounts on top of that.

Raises Questions about Contractual Rights

Policy makers may wish to consult legal counsel before designing a benefit linked to non-contractual rights language.

Statute specifies that the Legislature reserves the right to amend or repeal the Uniform COLA, and that future increases to the Uniform COLA are not a contractual right. The option does not specify whether the CPI-Based COLA would have similar language. Policy makers would need to specify whether or not the proposed new benefit is a contractual, or a non-contractual right. The implications of making the proposed new benefit a contractual right while leaving the Uniform COLA a non-contractual right are unclear. Also, non-contractual rights language similar to that used in the Uniform COLA is currently subject to litigation. Policy makers may wish to consult legal counsel before designing a benefit that is linked to non-contractual rights language.

Committee Activity

Staff briefed the full SCPP on this issue, including the original stakeholder proposals, at the September meeting. At the Executive Committee meeting that followed, the stakeholders requested the Committee allow them to revise the proposals under consideration. The Executive

Committee directed staff to brief the Full Committee on the revised stakeholder proposals, with revised pricing, in November.

Stakeholder Input

Correspondence from:

Public Employees for Pension Reform (PEPR)

Next Steps

The Committee may consider a variety of actions in response to the issue. Options include:

- Take no further action.
- Direct staff to draft legislation based on one or more of the stakeholder proposals.
- Study additional options.

Appendix A

History of Post-Retirement Adjustments in TRS 1 and PERS 1

Date	TRS 1	PERS 1
3/21/61		Minimum pension $900/year if retired at age 70 with 10 or more years of service $60/month if 15-19 years of service $70/month if 20-24 years of service $80/month if 25-29 years of service $90/month if 30 or more years of service
3/21/67		Minimum benefit increases to: $60/month if 12-15 years of service $90/month if 16-19 years of service $120/month if 20 or more years of service
7/1/67	Pension portion of benefit increased to $5.50/month/year of service if age 65 and not qualified for Social Security.	
3/25/69		Minimum benefit increases to: $75/month if 12-15 years of service $100/month if 16-19 years of service $130/month if 20 or more years of service
7/1/70	Minimum benefit revised to $5.50/month/year of service. Applicable to members retiring before 4/1/69. Applied to the pension portion of the benefit.	The following received for each $1 of pension by year of retirement: ‘49 - $1.5239 ‘56 - $1.3687 ‘63 - $1.2116 ‘50 - $1.5386 ‘57 - $1.3485 ‘64 - $1.1960 ‘51 - $1.5239 ‘58 - $1.3031 ‘65 - $1.1813 ‘52 - $1.4110 ‘59 - $1.2601 ‘64 - $1.1620 ‘53 - $1.3805 ‘60 - $1.2501 ‘65 - $1.1291 ‘54 - $1.3702 ‘61 - $1.2116 ‘66 - $1.0980 ‘55 - $1.3643 ‘62 - $1.2255 ‘67 - $1.0536
7/1/71		5.95% COLA applied to pension portion of the benefit if retired before 12/31/70.
7/1/72	5.9% COLA for all members retired before 7/1/71, plus an additional 5.4% for those retired between 7/1/69 and 6/30/70.	
4/25/73		Minimum benefit of $6.50/month/year of service. 3% permanent increase based on assets in excess of current liabilities.

Date	TRS 1	PERS 1
7/1/73	$3/month/year of service for retirees not eligible for Social Security.	Increase of 1.0609% if the member retired before 1972 and their service retirement allowance was adjusted in section (1) for adjustment made of 4/25/73.
7/1/74	11.9% pension increase for those retired on 6/31/70. 2.9% pension increase for those retired 7/1/70 - 6/30/73. 3% COLA on total allowance for those retired on 12/31/73.	3% COLA for those retired prior to 12/31/73.
7/1/75		3% COLA for those retired prior to 12/31/74.
7/1/76	Minimum pension benefit of $7.50/month/year of service if retired prior to 4/25/73.	3% COLA for those retired prior to 12/31/75.
7/1/77	Minimum pension benefit of $8.00/month/year of service if retired prior to 4/25/73.	3% COLA for those retired prior to 12/31/76.
7/1/78		3% COLA for those retired prior to 12/31/77.
7/1/79	Minimum pension benefit of $10/month/year of service for retirees of 7/1/79. Disability and survivor benefits as of 12/31/78, and service benefits as of 7/1/74 permanently increased by $0.8171 multiplied by the member's years of service.	Minimum pension benefit of $10/month/year of service for retirees of 7/1/79. 3% COLA for those retired prior to 12/31/78.
7/1/80		3% COLA for those retired prior to 12/31/79.
7/1/81		Excess earnings adjustment no longer in effect as employer contribution rate increased above rate on 4/24/73.
7/1/83	$0.74/month/year of service COLA to disability and survivor benefits being received on 12/31/82 and service retirement benefits being received on 7/1/78.	
7/1/86	Minimum benefit increased to $13.00/month/year of service.	
7/1/87	Permanent automatic 3% annual increase to the minimum benefit becomes effective. Minimum pension benefit increased to $13.50/month/year of service.	
7/1/88	Minimum pension benefit increased to $13.82/month/year of service.	
7/1/89	Minimum pension benefit increased by $1 to $14.91/month/year of service and then increased 3% to $15.36/month/year of service. Permanent automatic COLA enacted for retirees whose age 65 purchasing power had been reduced by more than 40%.	
7/1/90	Minimum pension benefit increased 3% to $15.72/month/year of service. 3% COLA for eligible retirees.	

<table>
<tr><th>Date</th><th>TRS 1</th><th>PERS 1</th></tr>
<tr><td>7/1/91</td><td colspan="2">Minimum pension benefit increased 3% to $16.19/month/year of service.
3% COLA for eligible retirees.</td></tr>
<tr><td>2/1/92</td><td colspan="2">The current benefits of those eligible for the COLA adjusted to be equal to 60% of their age 65 retirement allowance.</td></tr>
<tr><td>7/1/92</td><td colspan="2">Minimum pension benefit increased 3% to $16.68/month/year of service.
3% COLA for eligible retirees.</td></tr>
<tr><td>7/1/93</td><td colspan="2">Minimum pension benefit increased 3% to $17.18/month/year of service.
3% COLA for eligible retirees.
Continuation of special adjustment effective 2/92.
Temporary ad hoc COLA effective through 6/30/94, $3/month/year of service for those retired 5 years, who were 70 years of age, and did not receive a COLA in 1992.</td></tr>
<tr><td>7/1/94</td><td colspan="2">Minimum pension benefit increased 3% to $17.70/month/year of service.
3% COLA for eligible retirees.
Special adjustment effective 2/92 made permanent.
Temporary ad hoc COLA extended to 6/30/95. Provides $3/month/year of service to eligible retirees.</td></tr>
<tr><td>7/1/95</td><td colspan="2">Uniform Increase established. Initial increase of $0.59/month/year of service to be increased by 3% per year. Retirees are eligible for the Uniform Increase if they have been retired at least one year and are age 66 by 7/1 in the calendar year in which the annual increase is given, or if their retirement allowance is lower than the minimum benefit amount.
Minimum benefit increased to $24.22/month/year of service, and to automatically increase each year by the Annual Increase amount.
Temporary ad hoc COLA that had been extended to 6/30/95 made permanent.</td></tr>
<tr><td>7/1/98</td><td colspan="2">Gain-sharing established, providing even-year enhancements to the Annual Increase amount based on half the compound average investment returns in TRS 1 and PERS 1 plan assets over the previous four fiscal years that exceed 10%.</td></tr>
<tr><td>7/1/04</td><td colspan="2">$1,000 minimum benefit (before optional benefit payments) established for retirees with 25 years of service and at least 20 years of retirement. Does not include an automatic increase. Effectively sunsets after the regular minimum increases to $40/month/year of service.</td></tr>
<tr><td>7/1/06</td><td colspan="2">$1,000 minimum benefit (before optional benefit payments) extended to retirees with 20 years of service and at least 25 years of retirement. Automatic increase provided for $1,000 minimum of 3% per year.</td></tr>
<tr><td>7/1/07</td><td colspan="2">Uniform COLA eligibility changed to include all retirees who have been retired one year and will have attained age 66 by 12/31 of the calendar year in which the increase is given.</td></tr>
<tr><td>7/22/07</td><td colspan="2">Gain-sharing repealed after 2008 distribution. One-time increase in the Uniform COLA of $0.40*/month/year of service in lieu of future gain-sharing.

*Thirty-five cents of the increase payable 1/1/08; five cents payable on 7/1/09.</td></tr>
</table>

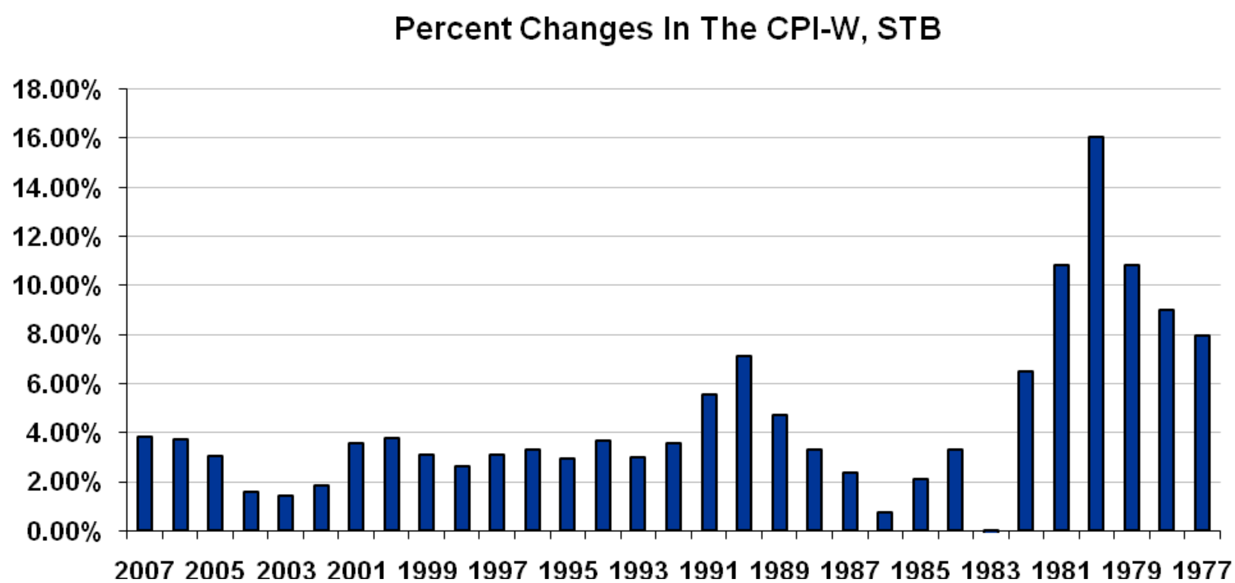
Appendix B

Consumer Price Index

Inflation is measured by the Consumer Price Index (CPI). The CPI records changes in the price of a set "market basket" of goods and services at different points in time. The U.S. Department of Labor publishes numerous indexes that measure inflation based on different market baskets and geographic regions. Each CPI produces a slightly different measure of inflation. The CPI most commonly used in Washington State's retirement systems is the Consumer Price Index for Urban Wage Earners and Clerical Workers for Seattle-Tacoma-Bremerton (CPI-W, STB).

An individual may experience inflation quite different from that measured by the CPI if the goods and services purchased by the individual do not closely match the market basket used by the CPI.

The following graph shows historical rates of inflation based on annual changes in the CPI-W, STB. Data for the graph is provided on the following page.



Percent Changes in the CPI-W, STB

Year	CPI	Change
2007	623.65	3.79%
2006	600.9	3.73%
2005	579.3	3.02%
2004	562.3	1.57%
2003	553.6	1.41%
2002	545.9	1.81%
2001	536.2	3.55%
2000	517.8	3.75%
1999	499.1	3.10%
1998	484.1	2.63%
1997	471.7	3.10%
1996	457.5	3.30%
1995	442.9	2.90%
1994	430.4	3.66%
1993	415.2	2.98%
1992	403.2	3.54%
1991	389.4	5.53%
1990	369.0	7.11%
1989	344.5	4.68%
1988	329.1	3.30%
1987	318.6	2.35%
1986	311.3	0.71%
1985	309.1	2.08%
1984	302.8	3.27%
1983	293.2	-0.27%
1982	294.0	6.48%
1981	276.1	10.84%
1980	249.1	16.08%
1979	214.6	10.85%
1978	193.6	9.01%
1977	177.6	7.96%

Year	CPI	Changes
1976	164.5	5.58%
1975	155.8	10.11%
1974	141.5	10.98%
1973	127.5	6.52%
1972	119.7	2.84%
1971	116.4	2.11%
1970	114.0	4.40%
1969	109.2	4.90%
1968	104.1	4.10%
1967	100.0	2.99%
1966	97.1	2.75%
1965	94.5	1.18%
1964	93.4	1.41%
1963	92.1	1.66%
1962	90.6	1.46%
1961	89.3	1.59%
1960	87.9	1.27%
1959	86.8	1.88%
1958	85.2	2.28%
1957	83.3	4.13%
1956	80.0	1.27%
1955	79.0	0.51%
1954	78.6	0.00%
1953	78.6	1.29%
1952	77.6	2.51%
1951	75.7	7.68%
1950	70.3	1.44%
1949	69.3	-0.43%
1948	69.6	8.24%
1947	64.3	13.20%
1946	56.8	

Source	U.S. Department of Labor, Bureau of Labor Statistics
CPI:	Urban Wage Earners and Clerical Workers (Current Series)
Seasonal:	Not Seasonally Adjusted
Area:	Seattle-Tacoma-Bremerton, Washington
Base:	Alternate (base period = 1967)
Item:	All Items

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Public Employees for Pension Reform

A coalition of Washington State Public Employee Unions and Retiree Associations serving active and retired state and public employees

TO: Select Committee on Pension Policy (SCPP)

FROM: Public Employees for Pension Reform (PEPR)

DATE: October 7, 2008

RE: Revised Proposals for Plan 1 COLA Improvement

RECEIVED
OCT 7 - 2008
Office of
The State Actuary

Members of the Public Employees for Pension Reform (PEPR) coalition appreciate the Select Committee on Pension Policy's (SCPP) 9/16/08 Work Session on Plan 1 Purchasing Power. The briefing by staff from the Office of the State Actuary (OSA) provided a much-needed update on the current status of Plan 1 pension benefits, as well as important information on policy and cost considerations related to the PEPR coalition's proposals for short and long-term Plan 1 COLA improvement. We also greatly appreciate the authorization by SCPP Executive Committee members for PEPR coalition members to put forth a revised set of proposals that would reduce costs from estimates on the original COLA improvement proposals.

In refection of the updated data regarding lost purchasing power, our continuing goal of broad-based COLA enhancement, and the budget challenges facing employers in the 2009-11 biennium and beyond, members of the PEPR coalition offer the following revised proposals for Plan 1 COLA improvement:

Key changes noted in **bold** print.

Short-Term Plan 1 COLA Improvement

New Supplemental Adjustment to the Uniform COLA's Annual Increase granted 7/1/09 based on the year of retirement:

- 1985-90 — ~~$0.75~~ **$0.35** per month/per years of service
  (approximate benefit increase of ~~$22.50~~ $10.50 per month for a retiree with *30 years of service*)
- 1980-84 — ~~$1.00~~ **$0.50** per month/per years of service
  (approximate benefit increase of ~~$30.00~~ $15.00 per month for a retiree with *30 years of service*)
- 1979 and earlier* — ~~$1.50~~ **$0.75** per month/per years of service
  (approximate benefit increase of ~~$45.00~~ $22.50 per month for a retiree with *30 years of service*)

Based on year of retirement, the design of the proposed benefit improvement is a variation of the '95 age based adjustments to provide a supplemental adjustment to the annual increase of the Uniform Plan 1 COLA. This option would provide a degree of relief to those who have been retired the longest, and have experienced the most severe losses in purchasing power, while acknowledging budget challenges facing employers.

Long-Term Plan 1 COLA Improvement

Replace Uniform "COLA" with a true *Cost-of-Living Adjustment* (COLA):

- based on 100% of the Consumer Price Index (CPI) up to 3% (banked)
- CPI: Urban Wage Earners & Clerical Workers, Seattle-Tacoma-Bremerton, WA – All Items
- prospective only
- paid/compounded annually
- ~~beginning 1 year after retirement~~ **beginning in July the retiree turns age 66** (to coincide more closely with COLA eligibility for Plans 2/3 and the current Uniform Plan 1 COLA)
- **CPI measured from date of retirement** (to coincide with methods of calculating the COLA for Plans 2/3)
- **annual benefit to be the greater of this CPI-based COLA or the Uniform COLA** (to ensure no loss of benefit).

This option would bring uniformity to COLA benefit design between systems and plans and protect the value of Plan 1 pension purchasing power while acknowledging budget challenges facing employers and the desire to contain COLA eligibility policy.

The PEPR coalition looks forward to continuing this dialogue with SCPP members to develop solutions to the critical issue of recovery of Plan 1 purchasing power.

Public Employees for Pension Reform (PEPR)

Washington State Federation of State Employees
Matt Zuvich, Chair – 306-352-7603

American Federation of Teachers of Washington
Washington Public Employees Association
Washington State Council of City & County Employees – Council 2
Retired Public Employees Council of Washington
Association of Washington School Principals
Washington Association of School Administrators
Public School Employees of Washington
Washington Education Association
Washington Education Association – Retired
Washington State School Retirees' Association

The Select Committee on Pension Policy

Plan 1 COLA Proposals

Darren Painter, Policy Analyst
November 18, 2008

Office of the State Actuary
"Securing tomorrow's pensions today."

What Is The Issue?

- SCPP asked to revisit PERS & TRS Plans 1 COLA
- Stakeholders seeking improvements
  - Proposed two changes
- Key policy questions
  - Is the current COLA sufficient?
  - If not
    - Who most needs an improved COLA?
    - What form should the COLA take?

Committee Activity

- Briefing in September
  - Background, policy, stakeholder proposals
- Stakeholders asked to revise proposals
- Work session on revised proposals today
  - Preliminary pricing
- No policy decisions made

Different COLAs Policies In Plans 1 & Plans 2/3

- Plans 1 provide a service-based "Uniform COLA" (UCOLA)
  - Design is compromise between adequacy of benefits, purchasing power protection, and affordability
  - Integrated with minimum benefits
- Plans 2/3 provide CPI-based COLA
  - Designed to protect purchasing power
- Differences linked to underlying plan design
  - Plan 1 provides reward for service
  - Plan 2/3 provides income replacement
    - Normal retirement age

Policy Highlights

- UCOLA help maintain the value of pensions
  - Provides more protection for retirees with lower salaries
  - Provides larger increases for some than a CPI-based COLA
- SCPP Goal 4 on purchasing power in Plans 1
  - To increase and maintain to extent feasible while providing long-term benefit security
- Benefit improvements for past service in Plans 1
  - Increase the unfunded past liability (UAAL)
  - Run counter to principle of intergenerational equity

Revised Stakeholder Proposals

- Short-term option
- Long-term option
- Stakeholders revised both options

Revised Short-Term Option

- Supplements existing Uniform COLA
- Grants additional increases based on year of retirement
  - 1985-1990 = $0.35*
  - 1980-1984 = $0.50*
  - 1979 and earlier =$0.75*

  **Dollars/month/year of service*
- Impacts nearly 33,000 retirees

Policy Implications: Revised Short-Term Option

- Larger increases to members retired longest
- Trade-off between ease of administration and precision in replacing purchasing power
- Results in different minimum benefits based on retirement date
  - Do members retired longer require larger minimum benefits?

Preliminary Total Employer Rate Increase

Revised Short-Term Option	
System	**Employer Rate Increase**
PERS	0.04%
TRS	0.09%
SERS	0.04%
PSERS	0.04%

Preliminary Fiscal Costs

Revised Short-Term Option	
Budget Impacts	*($ in millions)*
2009-2011	
Total GF-S	$6.6
Total Employer	15.6
25-Year	
Total GF-S	60.6
Total Employer	$160.9

These costs are preliminary and will be updated for any legislation based on this proposal.

Revised Long-Term Option

- Provide better of
  - Uniform COLA
  - CPI-based COLA like in Plan 2/3
- Proposed CPI-based COLA
  - CPI from retirement up to 3% maximum a year
  - Starts year recipient reaches age 66
  - Doesn’t make up for past inflation
- Impacts over 114,000 active, terminated vested, and retired members

Policy Implications: Revised Long-Term Option

- Generally prevents the further loss of purchasing power
- Does not diminish benefits
- CPI-based COLA provides similar value to Plan 2/3 COLA
- Raises questions about contractual rights
  - Uniform COLA is non-contractual
  - Creates uncertainty

Possible Next Steps

- Take no further action
- Draft legislation based on one or more stakeholder proposals
- Study additional options

7. DRS Technical Corrections

DRS Technical Corrections

Description of Proposal

- Repeals two obsolete sections of Plan 1 of the Teachers' Retirement System.
  - The disability reserve fund in RCW 41.32.360 is no longer used.
  - The death benefit fund in RCW 41.32.366 is no longer used.
  - The Department of Retirement Systems has paid death and disability benefits from the pension reserve fund since 1992.
- No fiscal impact.

SCPP's Procedural Options

- Sponsor as SCPP request legislation.
- Receive as information only and take no action.

Procedural History / Next Steps

The full SCPP has not been briefed on this proposal. However, there are no policy decisions to make with respect to the proposed corrections. The matter is set for public hearing and possible Executive Session at the November 18, 2008 meeting.

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Laura Harper 360-786-6145
Office of the State Actuary
October 23, 2008 (2:16 PM)

AN ACT Relating to repealing certain obsolete state retirement statutes; and repealing RCW 41.32.360 and 41.32.366.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

NEW SECTION. **Sec. 1.** The following acts or parts of acts are each repealed:

(1) RCW 41.32.360 (Basis of contributions to disability reserve fund) and 1991 c 35 s 47, 1963 ex.s. c 14 s 8, 1955 c 274 s 17, & 1947 c 80 s 36; and

(2) RCW 41.32.366 (Basis of contributions to death benefit fund) and 1991 c 35 s 48 & 1963 ex.s. c 14 s 10.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**11/4/08**	**DRS Technical Corrections**

WHAT THE READER SHOULD KNOW

The Office of the State Actuary ("we") prepared this draft fiscal note based on our understanding of the proposal as of the date shown above. We intend this draft fiscal note to be used by the Select Committee on Pension Policy (SCPP) throughout the 2008 Interim only. If a legislator introduces this proposal as a bill during the next Legislative Session, we will prepare a final fiscal note based on that bill language. The actuarial results shown in this draft fiscal note may change when we prepare our final version for the Legislature.

We advise readers of this draft fiscal note to seek professional guidance as to its content and interpretation, and not to rely upon this communication without such guidance. Please read the analysis shown in this draft fiscal note as a whole. Distribution of, or reliance on, only parts of this draft fiscal note could result in its misuse, and may mislead others.

RESULTS

There is no fiscal impact resulting from this proposal.

This proposal would repeal two obsolete sections of statute concerning Plan 1 of the Teachers' Retirement System: RCW 41.32.360 (Basis of contributions to disability reserve fund) and RCW 41.32.366 (Basis of contributions to death benefit fund). The auxiliary funds referenced in these statutes are no longer used. Since 1992, the Department of Retirement Systems has paid death and disability benefits from the pension reserve fund.

ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. This draft fiscal note has been prepared for the SCPP.
2. This draft fiscal note has been prepared, and opinions given, in accordance with Washington State law and accepted actuarial standards of practice as of the date shown on page 1 of this draft fiscal note.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. While this draft fiscal note is meant to be complete, the undersigned is available to provide extra advice and explanations as needed.

Matthew M. Smith, FCA, EA, MAAA
State Actuary

The Select Committee on Pension Policy

DRS Technical Corrections

Laura Harper, Policy and Research Services Manager

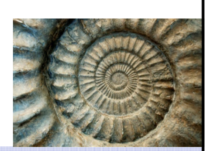
November 18, 2008

Office of the State Actuary

"Securing tomorrow's pensions today."

Proposal To Repeal Two Obsolete Statutes

- Proposal comes from Department of Retirement Systems (DRS)
- Two funds in TRS, no longer used
  - Disability fund, RCW 41.32.360
  - Death fund, RCW 41.32.366
- By statute, death and disability benefits paid from pension reserve fund since 1992



SCPP Technical Corrections Bills

- Proposed in long sessions
  - SCPP bills in 2005, 2007
  - OSA gathers input on potential cleanup legislation
- Examples
  - Repeal obsolete statutes
  - Correct errors (e.g., incorrect citations, omissions, clerical mistakes, double amendments)
- Parameters
  - Do not impact member benefits
  - No policy implications
  - No fiscal impact

Possible Next Steps

- Sponsor as SCPP request legislation
  - Bill draft available
  - Set for public hearing and possible action today
- Receive as information and take no action
  - Save for a future technical corrections bill

8. OSA Request Legislation

OSA Request Legislation

Description of Proposal

1. Clarifies how the State Actuary studies certain assumptions.
   - ❖ Total salary growth is an actuarial assumption with both economic and demographic components.
     - o Current statute can be read to suggest that components are studied at different times.
   - ❖ State Actuary studies components of total salary growth at the same time.
     - o Each component affects total.
     - o State Actuary studies components and makes recommendations as needed.
     - o New law would clarify this process.
2. Codifies current practice.
   - ❖ Experience studies are used to evaluate demographic assumptions.
   - ❖ Under current practice and based on experience study results, the State Actuary makes recommendations to the Pension Funding Council (PFC) concerning long-term demographic assumptions. The PFC considers these recommendations when adopting biennial contribution rates.
     - o Current statute does not require these steps.
       - ▪ Only requires State Actuary to <u>file</u> experience study results.
     - o New law would codify current practice.
3. Consistent with Actuarial Standards of Practice.
4. No fiscal impact.

SCPP's Procedural Options

1. Sponsor as SCPP request legislation.
2. Endorse as OSA request legislation.
3. Receive as information only and take no action.

Committee Activity / Next Steps

The full SCPP received a preview of this issue at its June meeting and a briefing at its October meeting. At the October Executive Committee meeting, the Chair, Vice Chair and Executive Committee Member Carlson recommended that the proposal be forwarded to the Legislature as 2009 SCPP request legislation. (Note: Three members of the Executive Committee were absent at this point so there was no motion.)

The matter is set for public hearing and possible Executive Session at the November meeting.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #:	Z-0222.1/09
ATTY/TYPIST:	LL:seg
BRIEF DESCRIPTION:	Addressing the state actuary's recommendations for assumptions used in the actuarial funding of the state retirement systems.

AN ACT Relating to the state actuary's recommendations for assumptions used in the actuarial funding of the state retirement systems; and amending RCW 41.45.030 and 41.45.090.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

Sec. 1. RCW 41.45.030 and 2007 c 280 s 1 are each amended to read as follows:

(1) Beginning September 1, 2007, and every two years thereafter, the state actuary shall submit to the council information regarding the experience and financial condition of each state retirement system, and make recommendations regarding the long-term economic assumptions set forth in RCW 41.45.035. When making recommendations regarding the general salary increase assumption, the state actuary may also consider the demographic components of total salary growth and make recommendations to the council concerning any changes to the demographic assumptions within total salary growth. The council shall review this and such other information as it may require.

(2) By October 31, 2007, and every two years thereafter, the council, by affirmative vote of four councilmembers, may adopt changes

to the long-term economic assumptions established in RCW 41.45.035. Any changes adopted by the council shall be subject to revision by the legislature.

The council shall consult with the economic and revenue forecast supervisor and the executive director of the state investment board, and shall consider long-term historical averages, in reviewing possible changes to the economic assumptions.

(3) The assumptions and the asset value smoothing technique established in RCW 41.45.035, as modified in the future by the council or legislature, shall be used by the state actuary in conducting all actuarial studies of the state retirement systems, including actuarial fiscal notes under RCW 44.44.040. The assumptions shall also be used for the administration of benefits under the retirement plans listed in RCW 41.45.020, pursuant to timelines and conditions established by department rules.

Sec. 2. RCW 41.45.090 and 2003 c 295 s 9 are each amended to read as follows:

(1) The department shall collect and keep in convenient form such data as shall be necessary for an actuarial valuation of the assets and liabilities of the state retirement systems, and for making an actuarial investigation into the mortality, service, compensation, and other experience of the members and beneficiaries of those systems. The department and state actuary shall enter into a memorandum of understanding regarding the specific data the department will collect, when it will be collected, and how it will be maintained. The department shall notify the state actuary of any changes it makes, or intends to make, in the collection and maintenance of such data.

(2) At least once in each six-year period, the state actuary shall conduct an actuarial experience study of the mortality, service, compensation, and other experience of the members and beneficiaries of each state retirement system((~~, and into the financial condition of each system~~)). The state actuary shall make recommendations to the council regarding the long-term demographic assumptions for the state retirement systems. Concurrently, when considering the demographic components of total salary growth, the state actuary may also study the general salary increase assumption and make recommendations to the council regarding any change to the noninflationary component of that

economic assumption. The council shall review the experience study results, the recommendations of the state actuary, and other information as it may require.

The results of each investigation shall be filed with the department, the office of financial management, the budget writing committees of the Washington house of representatives and senate, the select committee on pension policy, and the pension funding council. Upon the basis of such actuarial investigation the department shall adopt such tables, schedules, factors, and regulations as are deemed necessary in the light of the findings of the actuary for the proper operation of the state retirement systems.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**11/5/08**	**Z-0222.1**

WHAT THE READER SHOULD KNOW

The Office of the State Actuary ("we") prepared this draft fiscal note based on our understanding of the proposal as of the date shown above. We intend this draft fiscal note to be used by the Select Committee on Pension Policy (SCPP) throughout the 2008 Interim only. If a legislator introduces this proposal as a bill during the next Legislative Session, we will prepare a final fiscal note based on that bill language. The actuarial results shown in this draft fiscal note may change when we prepare our final version for the Legislature.

We advise readers of this draft fiscal note to seek professional guidance as to its content and interpretation, and not to rely upon this communication without such guidance. Please read the analysis shown in this draft fiscal note as a whole. Distribution of, or reliance on, only parts of this draft fiscal note could result in its misuse, and may mislead others.

RESULTS

There is no fiscal impact resulting from this proposal.

This proposal affects the processes around actuarial assumption-setting. First, the proposal would clarify how the State Actuary studies total salary growth. Total salary growth is an actuarial assumption with both economic and demographic components. The current statute could be read to suggest that the components are studied at different times. Under this proposal, the State Actuary is specifically authorized to study various components of total salary growth at the same time and make recommendations as needed.

The proposal also codifies current practice related to experience studies. Under current practice and based on experience study results, the State Actuary makes recommendations to the Pension Funding Council (PFC) concerning long-term demographic assumptions. The PFC considers these recommendations when adopting biennial rates. Current statute does not require these steps; it only requires the State Actuary to file the experience study results. The new law would codify current practice.

Both process changes are consistent with the Actuarial Standards of Practice.

ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. This draft fiscal note has been prepared for the SCPP.
2. This draft fiscal note has been prepared, and opinions given, in accordance with Washington State law and accepted actuarial standards of practice as of the date shown on page 1 of this draft fiscal note.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. While this draft fiscal note is meant to be complete, the undersigned is available to provide extra advice and explanations as needed.

Matthew M. Smith, FCA, EA, MAAA
State Actuary

The Select Committee on Pension Policy

OSA Request Legislation

Laura Harper, Policy and Research Services Manager

November 18, 2008

Office of the State Actuary

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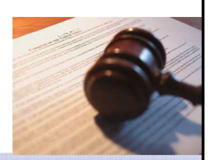
What Would The Bill Do?

- Clarify
  - How the State Actuary studies total salary growth
- Codify
  - Current practices related to experience study results
- Affects process only; no fiscal impact



Committee Activity

- Briefings in June and October
- Discussed at October Executive Committee meeting
  - Members favored sponsoring as SCPP legislation
  - No formal motion

Recap Of Proposed New Law

- Clarify how the State Actuary studies total salary growth
  - Study components at the same time
  - Make recommendations as needed
- Codify what happens when experience study is complete
  - State Actuary does not just <u>file</u> the results; State Actuary makes recommendations to the Pension Funding Council (PFC)
  - PFC reviews the recommendations
- Consistent with Actuarial Standards of Practice
- No fiscal impact

Possible Next Steps

- SCPP recommends proposal as SCPP request legislation
- Proposal proceeds as OSA request legislation
  - SCPP could endorse by motion and vote
  - SCPP could receive as information and take no action
- Set for public hearing and possible action today

9. SERS Past Part-time Service Credit

SERS Past Part-Time Service Credit

Description of Issue

In the past, some SERS members made contributions to the retirement system without receiving service credit. This occurred because contributions were required even if a member did not work enough hours to qualify for service credit. Current rules do not allow for such "non-credited" service.

SERS members have suggested that the current, more generous, service credit rules be retroactively applied to their non-credited past service.

Nearly 4,000 SERS members and over 15,000 members of other systems may have non-credited past service.

Policy Highlights

- Impacts more than SERS.
- Legislature has dealt with this before (1986 and 1991). Didn't change past non-credited service–except for some teachers.
- Differs from other retroactive benefit increases since contributions were already collected.
- A 2008 non-SCPP bill would have given SERS members credit for non-credited past service (HB 3182, no hearing).
- Idaho refunds contributions for non-credited service at retirement.

Policy Options

- **Refund Contributions for Non-credited Service.**
    - Doesn't require a retroactive policy change.
    - Consistent with past legislative actions in not retroactively changing service credit policy.
    - Less generous than granting service credit.
- **Apply Current Service Credit Rules to Past Service.**
    - Requires a retroactive policy change.
    - Inconsistent with past legislative actions.

- Ensures that members receive some service credit for any hours worked.
- May be targeted to educational employees only.

❖ **Apply Current Half-Time Service Credit Rules to Past Service.**

- Requires a limited retroactive policy change.
- Consistent with an earlier retroactive service credit change provided for teachers.
- Only impacts educational employees working at least half-time.

❖ **Take No Action.**

- Generally consistent with past legislative actions.
- No cost impact.

Executive Committee Recommendation

Apply current half-time service credit rules to past service.

Next Steps

Public hearing with possible executive action.

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SERS Past Part-Time Service Credit

Current Situation

Some members of the School Employees' Retirement System (SERS) who worked prior to January 1, 1987, have made contributions to the retirement system for part-time or partial-month work for which they did not receive any service credit. This occurred because, under the rules in place at that time, contributions were required even if a member did not work enough hours to qualify for service credit. This situation no longer occurs under current rules. *Service for which contributions were made but no service credit granted will be referred to as "non-credited" service throughout this paper.*

How Service Credit Works

Classified (i.e. non-teacher) school employees in retirement-system eligible positions make contributions to the retirement system on their salaries and receive service credit under applicable rules. Service credit is granted on either a monthly or yearly basis. Employees working in positions that are ineligible for retirement system participation (generally temporary or requiring few hours) do not pay any contributions or earn any service credit.

Currently, service credit is earned and contributions are made for any hours worked in an eligible position. Members who do not work enough hours to receive full service credit for the year or month will receive partial service credit for the year or month. Thus, under current rules, some service credit is always earned for periods in which contributions are made. See **Appendix A** for details of current service credit provisions.

How Did this Issue Come About?

The current rules allowing for partial service credit were put into place on September 1, 1991. Prior to that, service credit rules used to grant service credit on an all-or-nothing basis. Members who worked at least 90 hours in a month

In Brief

ISSUE

In the past, some SERS members have made contributions for work covered by the retirement system without receiving service credit. This occurred because contributions were required even if a member did not work enough hours to qualify for service credit. Current rules do not allow for such "non-credited" service.

Stakeholders are suggesting that the current, more generous service credit rules be retroactively applied to their past service.

MEMBER IMPACT

As of 2008, nearly 4,000 SERS members and over 15,000 members of other systems may have non-credited service.

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received full service credit for the month. Members who worked less than the minimum hours in a month did not receive any service credit for the month at all.

Some members might have made contributions for months in which service credit was not earned, depending on the contribution policy in effect. Prior to January 1, 1987, contributions were paid on all salaries in eligible positions whether or not service credit was earned. Beginning January 1, 1987, contributions were not required for any month in which service credit was not granted.

History

Service credit rules and contribution policies related to part-time and partial-month service credit have changed over time. Two bills are particularly relevant to an understanding of how this issue evolved. There has also been recent legislative activity on this issue.

Background on Service Credit and Contributions

Until 1987, contributions were required whether or not service credit was earned.

Prior to September 1, 1991, partial service credit was generally not provided in Washington State retirement systems.* However, until 1987, members were required to make contributions on salaries earned in an eligible position—whether or not service credit was also earned for the month.

All classified school employees were covered by the Public Employees' Retirement System (PERS) prior to 2000, and their service credit was granted under PERS rules. In 2000, classified school employees in PERS 2 were transferred to SERS. Classified school employees in PERS 1 remained in PERS.

**Except for Plan 1 of the Teachers' Retirement System, which did provide partial service credit at that time.*

Contribution Policy Changed in 1987

In 1986, a bill was passed that changed the contribution policy in relation to service credit for PERS, the Teachers' Retirement System (TRS), and the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF). (See Chapter 268, Laws of 1986.) Under the new policy, no

After 1987, contributions weren't required unless service credit was earned.

member or employee contributions were required for any calendar month in which the member did not receive service credit. This change went into effect January 1, 1987, and did not apply to contributions made prior to the effective date. Ultimately, the provision was not administrable due to limitations in the way payrolls were processed.

JCPP Studied Part-Time Employment in 1990

In 1990, the Joint Committee on Pension Policy (JCPP) studied issues related to part-time employment. The JCPP looked at retirement benefits for job-share and other part-time positions as well as current and past contribution requirements for such positions. The JCPP recommended legislation on this topic for the 1991 session.

Partial Service Credit Rules Established in 1991

In 1991, a version of the JCPP's bill on part-time employment passed the Legislature (Chapter 343, Laws of 1991). This bill made several changes related to service credit including:

In 1991, service credit was granted for all work in an eligible position.

- ❖ Setting forth a new legislative retirement policy that persons hired into eligible positions shall earn some service credit for any service rendered.
- ❖ Establishing the current structure for granting partial service credit for service rendered <u>after</u> September 1, 1991, in PERS, TRS 2, and LEOFF 2.
- ❖ Requiring refunds of contributions paid on and after January 1, 1987, for non-credited service. These refunds were made to members of PERS, TRS 2, and LEOFF 2. (This provision ensured compliance with the earlier contribution policy change.)
- ❖ Granting half-time service credit for TRS 2 members who worked under half-time contracts prior to December 31, 1986.

Recent Legislation on this Issue

A non-SCPP bill was introduced in 2008 that would have given SERS members non-credited past service.

During the 2008 Legislative session, a non-SCPP bill was introduced that dealt with non-credited past service for SERS members. HB 3182 would have allowed active SERS members to receive service credit for any non-credited service in an eligible position prior to September 1, 1987. The bill would allow service credit to be granted for those months based on current service credit rules; no additional contributions would be required. The fiscal note indicated a cost to the system and a rate impact in the current biennium. This bill did not receive a hearing.

Example

Sally is a food service worker for a school district. She worked part-time for the district between 1978 and 1987 before becoming a full-time employee. Sally's part-time position was eligible for participation in the retirement system. During the years that Sally worked part-time, she made contributions to the system on her earnings each month. During some months Sally was not able to work the 90 hours required to receive service credit under the rules in place at that time. For these months, Sally received no service credit but still paid her contributions to the system. These non-credited months were often months with fewer scheduled classroom days such as December, April, and June.

Policy Analysis

Impact on Members

The impact of non-credited service varies based on a couple of factors. One factor is whether members draw a pension from the plan and the other factor is what plan they are in.

Some members receive value from contributions for non-credited service, while others do not.

Non-credited service is not used in the calculation of pensions. Members with non-credited service who receive their contributions back with interest do get added value from contributions made for that service. Included in this group are Plan 3 members, and Plan 2 members who withdraw from the system (hence giving up their rights to a pension). In contrast, Plan 2 members who go on to receive a pension do not get any added value from contributions for non-credited service. In effect, these Plan 2 members end up paying more for their pension. However, they will still receive back more in pension payments than they paid in contributions. This is because pensions are also paid for by employer contributions and investment earnings.

Other Examples of Paying without Adding Value

The previous section explored how Plan 2 members with non-credited past service pay more for their pension without receiving any added value. There are other examples within Washington's retirement systems of members paying without adding value to their retirement benefit.

There are other examples in Washington's systems of members paying without receiving added value.

One example is the recently enacted subsidized early retirement factors for Plans 2/3 members with 30 years of service. All Plan 2 members will pay for this through higher contribution rates. However, some members will never be able to take advantage of the new factors because they won't earn the required service prior to age 65.

Service credit rules provide another example. Members who work more than the minimum number of hours required for full service credit effectively pay extra for their service. They pay contributions on all hours worked over the minimum but receive no additional service credit.

To illustrate, consider two SERS members. One member works 90 hours in a month, the other works 160 hours. Both members contribute for all hours worked and both members receive exactly one month of service credit. Salary considerations aside, the member who worked 160 hours will not receive any extra pension value for the contributions made for hours worked over 90.

Other Washington Plans

Over 15,000 non-SERS members might have non-credited past service.

The Department of Retirement Systems estimates that, as of April 2008, over 15,000 members of the state's other retirement systems might have non-credited past service. This includes both active and inactive, non-retired members.

Members of PERS, TRS 2, and LEOFF 2 who worked prior to January 1, 1987, might have contributed to the retirement system during months in which they did not work enough hours to earn service credit. PERS members are the most likely to be impacted since there are more part-time positions in PERS than the other systems. (Note: Impacted Plan 2 members of PERS and TRS may have since transferred to Plan 3.)

Current and future members of LEOFF Plan 1 and the Washington State Patrol Retirement System (WSPRS) might be impacted as well. LEOFF Plan 1 and WSPRS do not provide partial service credit. Members in these plans who work less than 70 hours a month in an eligible position do not receive any service credit for the month. However, they are still required to make contributions for the month. Since these plans are only open to full-time employees, members are most likely impacted if they are hired near the end of a month or leave near the beginning.

While this issue may impact members of other systems, only SERS members are seeking a solution at this time.

Other States

Idaho refunds contributions for non-credited service.

Idaho is the only one of ten Washington peer states in which classified school employees might be required to make contributions to a defined benefit plan without earning service credit. However, any contributions made for non-credited service are refunded to the member with interest when they withdraw or retire from the system. Members who retire receive the refunded contributions in addition to their service-based pension. Generally, only members who withdraw from the system can have their contributions refunded (as with Plans 1/2 of Washington's systems).

Implications of Retroactive Policy Changes

This issue illustrates what often happens when retirement policy is changed midstream. Inconsistencies might be created in benefits among various generations of workers. Consequently, members may seek to have the more favorable policy applied to past service. In this instance, members are suggesting that the current, more generous, service credit rules be applied to service rendered prior to when the rules were adopted. Changes applied to past service are often referred to as retroactive changes.

What happens when a benefit change is retroactively applied? In most cases, the cost of the improvement is spread to future workers and taxpayers since the benefit was not funded when it was earned. However, this issue differs in that contributions were collected while the member was working, but no additional pension benefit was provided.

It could be claimed that non-credited past service has already been paid for.

While it could be claimed that members and taxpayers have already paid for the cost of the non-credited past service, there is still a cost to grant this service today. This is because the retirement system has already realized a gain for non-credited service. (The system "gains" when contributions are collected but no pension benefit is provided.) There will be a cost to the retirement system if the prior gains realized for non-credited service are given back in new benefit improvements.

Legislative Precedent on Non-Credited Past Service

With one exception, the Legislature has chosen to not retroactively apply a solution.

At least twice, the Legislature has had the opportunity to address the issue of non-credited past service. With one limited exception, the Legislature has chosen to not retroactively apply a solution. One opportunity was in 1986 when the Legislature established the policy that contributions were not required when service credit was not granted. At that time, the Legislature did not require a refund of contributions for past non-credited service. A second opportunity occurred in 1991 when the Legislature established the policy that persons hired into eligible positions shall earn service credit for all service rendered. The resulting new service credit rules were not applied to prior service. (The Legislature created a special service credit rule applied retroactively applied to half-time teachers.)

Why not make Policy Changes Retroactive?

There are many reasons that policy makers may not apply a policy change retroactively. It might be a matter of practicality: it costs too much or is too difficult to administer. Policy makers may also be concerned about maintaining fairness across generations by not shifting costs to future generations (less of an issue with non-credited service). Another reason is that policy makers may wish to support the flexibility of the retirement systems. Requiring every policy change to apply retroactively might hamper the ability of policy makers to adapt retirement systems to changing circumstances.

Implications for Recent SCPP Work on Service Credit

Retroactive changes for non-credited past service may lead to calls for the recent TRS and SERS half-year contract changes to be applied retroactively as well. In 2007, the SCPP recommended new, more generous service credit rules for teachers and school employees working half-year contracts. The changes that were recommended by the SCPP and passed by the Legislature did not apply to prior service.

Policy Implications of HB 3182

HB 3182 requires a retroactive application of service credit rules and only applies to SERS.

HB 3182 is a non-SCPP bill introduced in 2008 that addresses the issue of non-credited past service. (Refer to the **History** section of this paper for a more complete description.) This bill requires a retroactive application of current service credit rules and only applies to active SERS members. The earlier discussion of the policy implications of retroactive changes and impacts on other Washington retirement systems apply to HB 3182.

Also, there is likely a technical problem with the date used in the bill draft for granting non-credited past service. The date used in the bill (September 1, 1987), falls after the date when contributions for non-credited service were refunded (January 1, 1987).

Conclusion

The issue of non-credited past service has implications around retroactive policy changes and equity across systems. It also raises questions about charging members without providing additional value in retirement benefits. The issue was first identified many years ago and the Legislature has had opportunities to address it. A bill was introduced in 2008 that proposes one possible solution for some impacted members. The state of Idaho found a different way to address non-credited service. SCPP members may wish to consider both these and other options in response to this issue.

Policy Options

The way policy makers respond to this issue will likely depend upon how they view the issue. Policy makers may view this in one of two ways:

Policy makers may view this issue in one of two ways.

- As a contribution policy issue.
- As a service credit issue.

Policy makers who view this as a contribution policy issue may be more inclined to consider refund options. Policy makers who view this as a service credit issue may be more inclined to consider options that grant additional service credit. No matter what their view, some policy makers may be inclined to take no action on this issue for various policy reasons.

Policy options for each view are discussed below. These options are not necessarily mutually exclusive. Policy makers may elect to provide a combination of options that grant refunds in some cases and grant service credit in others.

Service credit options are limited to those that retroactively apply current service credit rules to periods of past service. Other service credit approaches touch on the fundamental policies of how service credit should be awarded. This is a much larger issue with potentially greater impacts and very different policy considerations.

The policy options apply to a broader group of members than just SERS.

This issue was originally brought before the Legislature as a SERS issue. Subsequent research by staff revealed that non-credited service impacts members of most Washington plans. The policy options provided are designed to apply to a broader group of members than just SERS.

Preliminary pricing for each of the policy options was provided at the October meeting.

Option1: Refund Contributions for Non-Credited Service

This option provides a refund of contributions with interest at retirement for members who made contributions for a month in which they did not receive any service credit.

This option does not require a retroactive policy change, which is consistent with past legislative actions.

This option has several broad policy implications. It does not require a retroactive policy change, which is consistent with past legislative actions. This option ensures that members will receive some benefit for all contributions made—though refunds are less generous to members than granting additional service credit. In addition to taking care of past, non-credited service, this option would address future non-credited service in those plans where it may still occur—without opening up the issue of service credit in general. This option will not lead to earlier retirements because it does not impact service credit. This option is relatively easy to administer and refunds would be provided without requiring the member to separately apply or provide proof of hours worked.

This option impacts Plan 1 and Plan 2 members of PERS, TRS, SERS, LEOFF, and WSPRS. Plan 3 members currently receive their contributions with interest if they retire. Other systems are not impacted by non-credited service.

Option 2: Apply Current Service Credit Rules to Past Service

This option retroactively applies current service credit rules to periods of service prior to January 1, 1987, similar to the 2008 Legislation (HB 3182).

This option requires a retroactive policy change and is a departure from past legislative actions.

This option has several broad policy implications. It requires a retroactive policy change by applying current service credit policy to periods of past service rendered under different policy. This is a departure from the actions of past Legislatures that generally didn't choose to retroactively apply service credit rules. (See the **Policy Analysis** section for a more thorough discussion of retroactive policy changes.) This option is the most generous to members. It ensures that members receive some service credit for any hours worked. This option may lead to earlier retirements since it increases service credit and service credit is a factor in the ability to access improved retirement benefits.

Service credit may be granted for all non-credited service, or limited to non-credited service with an educational employer. One policy reason for limiting it to educational employment is that part-time educational employees may have been disadvantaged due to the nature of educational employment. During some months, part-time educational employees may not have been able to work enough hours to earn service credit under the past rules because schools were closed for holidays and other breaks.

This option would only apply to PERS, TRS 2/3, SERS, and LEOFF 2. These are the only plans where service credit policy was changed to address non-credited service.

Option 3: Apply Current Half-Time Service Credit Rules to Past Service

This option is similar to Option 2 except that it retroactively applies only the current *half-time* service credit rules for educational employees to periods of past educational service.

This option allows members who worked for an educational employer prior to January 1, 1987, to receive six months of service credit if they worked at least 630 hours during a full school year.

This option is consistent with an earlier retroactive service credit change provided for teachers.

This option is consistent with a retroactive service credit change that was provided for half-time teachers in 1991 (see **History** section). In other respects, this option has broad policy implications similar to Option 2. This option is less generous than Option 2 since it only impacts members who were working at least half-time. Members working less than half-time will not benefit under this option.

This option would only apply to members in PERS Plans 2/3 and SERS Plans 2/3. Half-time service credit rules only apply to Plans 2/3 educational employees. Non-credited past service for half-time teachers was addressed in 1991.

Option 4: Take No Action

Policy makers may choose to take no action for a variety of reasons.

Policy makers who view this as a service credit issue may choose to take no action if they want to avoid retroactive policy changes or are not overly concerned that prior service credit rules were not as generous as they could have been.

Policy makers who view this as a contribution issue may choose to take no action for a couple of reasons related to the underlying plan design:

- The benefits in a Defined Benefit (DB) plan like the Plans 1 and Plans 2 are not determined by the contributions made.
- It is not uncommon in a DB plan for members to pay additional contributions without adding additional value to their retirement benefits.

This option has no cost impact and is consistent with the general approach taken by the Legislature in the past.

Executive Committee Recommendation

At the October meeting, the Executive Committee recommended Option 3: *Apply current half-time rules to past service.*

Committee Activity

Staff first briefed the full committee on this issue at the June meeting. The Executive Committee directed staff to develop new policy options—including Option 3—and bring those options back to the full committee with pricing.

Staff briefed the full committee on the policy options at the October meeting. Following, the Executive Committee recommended that the full SCPP consider Option 3 for possible executive action at the November meeting.

Stakeholder Input

Correspondence from:

Carey Ensign, (e-mail and related attachment), received 1/30/2008.

Next Steps

Public hearing with possible executive action.

Bill Draft

An OSA bill draft to implement Option 3 is attached.

Draft Fiscal Note

Attached.

Appendix A
Service Credit Rules

Plans 2/3 Service Credit Rules

Educational Employees

Plan 2/3 members working for an educational employer (includes all SERS, all TRS, and some PERS members) earn service credit as follows*:

- ❖ At least 810 hours worked in a full school year = 12 months of service credit.
- ❖ At least 630 hours but less than 810 hours worked in a full school year = 6 months of service credit.
- ❖ At least 630 or more hours worked in five months of a six month period within a school year = 6 months of service credit.

Educational employees who work less than a full school year or less than 630 hours earn service credit on a month by month basis as described for non-educational employees.

Non-Educational Employees

Plans 2/3 members working for non-educational employers (includes PERS and LEOFF) earn service credit on a month by month basis as follows:

- ❖ 90 hours or more in a month = 1 month of service credit.
- ❖ At least 70, but less than 90 hours in a month = ½ month of service credit.
- ❖ Less than 70 hours in a month = ¼ month of service credit.

**Note: Members are awarded service credit under whichever rule provides the most service credit.*

PERS Plan 1 Service Credit Rules

Educational Employees

PERS 1 members working for an educational employer earn one year of service credit if they work at least 630 hours in a full school year.

Non-Educational Employees

PERS 1 members working for non-educational employers receive service credit on a month-by-month basis as follows:

- 70 hours or more in a month = 1 month of service credit.
- Less than 70 hours in a month = ¼ month of service credit.

O:\SCPP\2008\11-18-08 Full\9.SERS_Past_PT_Svc_Credit_Issue_Paper.doc

Hyde, Elizabeth

From: Harper, Laura
Sent: Friday, April 11, 2008 10:52 AM
To: Hyde, Elizabeth; Winner, Charlene
Cc: Burkhart, Kelly; Smith, Matt
Subject: FW: HB 3182

Attachments: HOUSE BILL 3182.doc

HOUSE BILL 3182.doc (26 KB) Please incorporate this into the SCPP correspondence log and bring copies of the e-mail and attachment to the Tuesday, April 15th meeting.

Thank you!

-----Original Message-----
From: Smith, Matt
Sent: Wednesday, January 30, 2008 4:15 PM
To: Harper, Laura
Cc: Burkhart, Kelly
Subject: FW: HB 3182

---- Original Message ----
From: "Dave Westberg" <iuoe609@qwestoffice.net>
Date: 1/30/08 3:33 pm
To: "Smith, Matt" <Smith.Matt@leg.wa.gov>
Cc: "Conway, Rep. Steve" <Conway.Steve@leg.wa.gov>
Subj: Fw: HB 3182
Matt

Please put this issue on the agenda for the upcoming interim.

Thank you

Dave Westberg

-----Original Message-----
From: "Tim & Carey Ensign" <tcensign@msn.com>

Date: Tue, 29 Jan 2008 19:36:31
To:<iuoe609@qwestoffice.net>
Subject: Fw: HB 3182

----- Original Message -----
From: Tim & Carey Ensign <mailto:tcensign@msn.com>
To: iuoe609@questoffice.net <mailto:iuoe609@questoffice.net>
Sent: Tuesday, January 29, 2008 7:30 PM
Subject: HB 3182

David - thank you for you call today. I am very excited that you will be following and helping with this bill. Please keep me updated on it's progress.

Attached is an informational piece I put together for my local chapter president, to outline the background on this bill. Please let me know if there is something I can do to help.

Carey Ensign
home - 360-871-3127
work - 360-443-3316
ensign@skitsap.wednet.edu <mailto:ensign@skitsap.wednet.edu>
tcensign@msn.com <mailto:tcensign@msn.com>

HOUSE BILL 3182

On January 22, 2008, House Bill 3182 was introduced in the Washington State House of Representatives by Representative Patricia Lantz of the 26TH District. House Bill 3182 would authorize application for past part-time service credit for members of the School Employees' Retirement System. To view the text of the bill, go to the Washington State Legislature website, click on Bill Information, and search for 3182.

Background:

In 1977, PERS (Public Employees Retirement System) Plan II was created. Prior to Plan II, PERS Plan I required 70 hours per month for a month's service credit. The threshold for service credit changed to 90 hours per month in PERS Plan II. Certificated school employees (teachers) and classified school employees (secretaries, custodians, bus drivers, etc.) were members of the PERS I and PERS II retirement systems. Many school districts did not pick up on the change from 70 hrs. to 90 hrs., and erroneously continued to consider employees eligible for PERS II at the threshold of 70 hours. Many part-time school employees across the state were paying into the PERS II retirement system, as well as the school districts on their behalf. The Washington State Department of Retirement Systems accepted these contributions and sent yearly statements to employees. These statements, however, did not include a summary of service credit earned, so there was no way for the employee to know that they were not earning service credit for all months worked. A DRS audit in 1984 revealed these errors. However, those employees identified in the audit (and, by 1984 were working more hours and, thus, eligible for service credit in PERS II) were not notified of their prior missing service credit. An employee of the South Kitsap School District discovered this problem in 1985 and contacted the Public School Employees (PSE) of Washington, the union representing classified school employees in her school district. PSE filed a class action lawsuit in the Superior Court of Thurston County, seeking a remedy for all school employees affected. The lawsuit was put on hold at the request of DRS to pursue an administrative solution. After several years, PSE reactivated the lawsuit when no satisfactory solution was found.

In 1991, the legislature enacted a statute allowing PERS Plan II members to earn less than one month's service credit if they did not work the requisite 90 hours. Prior to that time, it was all or nothing. That is, if you worked 89 hours in a month, you received zero retirement service credit for that month in Plan II. The partial service credit statue of 1991 was applied retroactively for teachers, but not classified employees.

In June of 1998, Public School Employees of Washington appeared before the Division II Court of Appeals regarding the case brought by PSE a number of years prior. PSE challenged the DRS interpretation of the partial service credit statute which DRS said applied only prospectively. PSE asked the Court of Appeals to apply the statute retroactively for classified school employees as it was applied retroactively for teachers. The Appeals Court acknowledged the unfairness, however, ruled that the courts have no authority to read retroactivity into the statute. That decision was the end of the line for a remedy through the court system.

The only avenue remaining is a legislative fix. Money from both employees and employers has been in the retirement system al these years and should rightfully benefit those employees. House Bill 3182 would solve this problem.

Darren Painter 786-6155
OSA
November 7, 2008 (4:46 PM)

AN ACT Relating to granting half-time service credit for half-time educational employment prior to January 1, 1987, in the plans 2 and 3 of the school employees' retirement system and the public employees' retirement system; and adding a new section to chapter 41.35 RCW and chapter 41.40 RCW.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

NEW SECTION. **Sec. 1.** A new section is added to chapter 41.35 RCW to read as follows:

(1) By no later than December 31, 2010, the department shall recalculate service credit for periods of qualifying prior service by an eligible member, as provided for in this section.

(2) An eligible member is a member who is active in the retirement system and who earns service credit after the effective date of this act and before September 1, 2010.

(3) A qualifying period of prior service is a school year prior to January 1, 1987 in which the member:

(a) Was employed in an eligible position by a school district or districts, educational service district, the state school for the deaf, the state school for the blind, an institution of higher education, or a community college; and

(b) Earned earnable compensation for at least six hundred thirty hours as determined by the department; and

(c) Received less than six months of service credit; and

(d) Has not withdrawn service credit for the school year or has restored any withdrawn service credit for the school year.

(4) The department shall recalculate service credit for qualifying periods of prior service for an eligible member as follows:

(a) The member shall receive one-half service credit month for each month of the period from September through August of the following year if he or she earned earnable compensation during that period for at least six hundred thirty hours as determined by the department, and was employed nine months of that period.

(b) A member's service credit shall not be reduced under this section for a qualifying period of prior service.

NEW SECTION. **Sec. 2.** A new section is added to chapter 41.40 RCW to read as follows:

(1) By no later than December 31, 2010, the department shall recalculate service credit for periods of qualifying prior service by an eligible member, as provided for in this section.

(2) An eligible member is a member of Plan 2 or Plan 3 who is active in the retirement system and who earns service credit after the effective date of this act and before September 1, 2010.

(3) A qualifying period of prior service is a school year prior to January 1, 1987 in which the member:

(a) Was employed in an eligible position by a school district or districts, educational service district, the state school for the deaf, the state school for the blind, an institution of higher education, or a community college; and

(b) Earned earnable compensation for at least six hundred thirty hours as determined by the department; and

(c) Received less than six months of service credit; and

(d) Has not withdrawn service credit for the school year or has restored any withdrawn service credit for the school year.

(4) The department shall recalculate service credit for qualifying periods of prior service for an eligible member as follows:

(a) The member shall receive one-half service credit month for each month of the period from September through August of the following year if he or she earned earnable compensation during that period for at least six hundred thirty hours as determined by the department, and was employed nine months of that period.

(b) A member's service credit shall not be reduced under this section for a qualifying period of prior service.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**11/7/08**	**Past Part-Time Service Credit**

WHAT THE READER SHOULD KNOW

The Office of the State Actuary ("we") prepared this draft fiscal note based on our understanding of the proposal as of the date shown above. We intend this draft fiscal note to be used by the Select Committee on Pension Policy, throughout the 2008 Interim only. If a legislator introduces this proposal as a bill during the next Legislative Session, we will prepare a final fiscal note based on that bill language. The actuarial results shown in this draft fiscal note may change when we prepare our final version for the Legislature.

We advise readers of this draft fiscal note to seek professional guidance as to its content and interpretation, and not to rely upon this communication without such guidance. Please read the analysis shown in this draft fiscal note as a whole. Distribution of or reliance on only parts of this draft fiscal note could result in its misuse, and may mislead others.

SUMMARY OF RESULTS

This proposal grants half-time service credit to certain Plan 2/3 members who worked half-time for an educational employer during school years prior to January 1, 1987.

Impact on Pension Liability

(Dollars in Millions)	**Current**	**Increase**	**Total**
Today's Value of All Future Pensions	$67,081	$0.2	$67,081
Earned Pensions Not Covered by Today's Assets	$4,957	$0.0	$4,957

Impact on Contribution Rates: (Effective 09/01/2009)

2009-2011 State Budget	**PERS**	**SERS**
Employee (Plan 2)	0.00%	0.00%
Employer:		
Current Annual Cost	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%
Total	0.00%	0.00%

Budget Impacts

(Dollars in Millions)	**2009-2011**	**2011-2013**	**25-Year**
General Fund-State	$0.0	$0.0	$0.1
Total Employer	$0.0	$0.0	$0.4

See the Actuarial Results section of this draft fiscal note for additional detail.

WHAT IS THE PROPOSED CHANGE?

Summary of Change

This proposal impacts the following systems:

- Public Employees’ Retirement System (PERS) Plans 2/3
- School Employees’ Retirement System (SERS) Plans 2/3

This proposal grants half-time service credit to certain PERS and SERS Plan 2/3 members who worked half-time for an educational employer during school years prior to January 1, 1987.

This proposal requires the Department of Retirement Systems (DRS) to recalculate service credit for periods of qualifying prior service by an eligible member. An eligible member is a Plan 2/3 member who is active in the retirement system and earns service credit after the effective date of the bill and before September 1, 2010. A qualifying period of prior service is a school year prior to January 1, 1987, in which the member:

- Was employed in an eligible position by one of the following employers: school districts, educational service districts, the state school for the deaf, the state school for the blind, institutions of higher education, or community colleges.
- Worked at least 630 hours.
- Received less than six months of service credit.
- Has not withdrawn service or has restored any withdrawn service.

Effective Date: 90 days after session

What Is The Current Situation?

Currently, Plan 2/3 members who work for an educational employer earn service credit as follows:

- At least 810 hours worked in a full school year = 12 months of service.
- At least 630 but less than 810 hours worked in a full school year = 6 months of service.
- At least 630 hours worked in five months of a six month period within a school year = 6 months of service.

Working less than a full school year or less than 630 hours: service credit is calculated on a month to month basis as follows:

- 90 hours or more in a month = 1 month of service.
- At least 70 but less than 90 hours in a month = ½ month of service.
- Less than 70 hours in a month = ¼ month of service.

Prior to January 1, 1987, Plan 2/3 members who worked for educational employers received 12 months of service credit if they were continuously employed for 9 months and worked at least 90 hours a month in at least 9 months of the school year. If they did not qualify to receive 12 months of service credit, they received 1 service credit month for each month of 90 hours worked. No service was awarded for any month of less than 90 hours. Members and employers made retirement contributions on all salary, regardless of the amount of service credit earned, if any.

Who Is Impacted And How?

We estimate this proposal could affect 192 active and vested terminated members out of the total 227,473 active and vested terminated members of these systems through improved benefits. Furthermore, we expect 132 active members will actually receive improved benefits.

We estimate this proposal will increase the benefits for a typical member by providing an increased retirement benefit to current active members. The average member affected by this proposal has a salary of $30,000 and will receive 0.25 years of additional service. This will increase their initial unreduced retirement benefit by $150 per year.

This proposal impacts all 138,392 active Plan 2 members of these systems through increased contribution rates. This proposal will not affect member contribution rates in Plan 3 since Plan 3 members do not contribute to their employer-provided defined benefit.

See Appendix A of this draft fiscal note for more details on members impacted.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This proposal has a cost since it allows active educational employees of PERS and SERS Plans 2/3 to have periods of half-time service credit earned prior to January 1, 1987, credited to their retirement account. This will increase their retirement benefit by the additional service provided under this proposal.

Who Will Pay For These Costs?

The affected members, who did not receive the half-time service credit prior to January 1, 1987, made contributions commensurate with the effective contribution rate. Therefore, these individuals already made the appropriate contributions. The entire system will provide for any additional costs through increased contribution rates.

HOW WE VALUED THESE COSTS

Assumptions We Made

We assumed all 132 current active members will receive the increase in service credit as provided under this proposal. Please see the Sensitivity Analysis section for how the results change when vested terminated members receive the increase in service credit.

Otherwise, we developed these costs using the same assumptions as disclosed in the June 30, 2007 Actuarial Valuation Report (AVR).

How We Applied These Assumptions

DRS identified the affected members in their database and provided the information to us. We isolated these members in our valuation data and increased their service by the additional service credits provided by DRS. The resulting change in service provides the source of the increase in actuarial liabilities, contribution rates, and fiscal costs.

Otherwise, we developed these costs using the same methods as disclosed in the AVR.

We used the Aggregate actuarial funding method to determine the fiscal budget changes for current plan members.

Special Data Needed

DRS provided special data for this proposal. The data indicated the number of months of service credit members received prior to January 1, 1987, under the half-time service credit rules at that time. The data also provided the number of months of service credit members would have received for the same period of service under the current half-time service credit rules.

For more detail please see Appendix A.

ACTUARIAL RESULTS

How The Liabilities Changed

This proposal will impact the actuarial funding of PERS and SERS Plans 2/3 by increasing the present value of future benefits payable under the systems as shown below.

Impact on Pension Liability

(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits			
(The Value of the Total Commitment to all Current Members)			
PERS 2/3	**$20,634**	**$0.0**	**$20,635**
SERS 2/3	**$2,698**	**$0.2**	**$2,698**
Unfunded PUC Liability			
(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)			
PERS 2/3	**($2,470)**	**$0.0**	**($2,470)**
SERS 2/3	**($443)**	**$0.2**	**($443)**

Note: Totals may not agree due to rounding.

How The Present Value of Future Salaries (PVFS) Changed

This proposal will impact the actuarial funding of PERS and SERS Plans 2/3 by decreasing the PVFS of the members of the systems as shown below.

Present Value of Future Salaries			
(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Future Salaries			
(The Value of the Future Salaries Expected to be Paid to Current Members)			
PERS 2	$56,420	$0.0	$56,420
PERS 3	11,717	0.0	11,717
PERS 2/3	**$68,137**	**$0.0**	**$68,137**
SERS 2	$3,837	$0.0	$3,837
SERS 3	7,153	0.0	7,153
SERS 2/3	**$10,990**	**$0.0**	**$10,990**

Note: Totals may not agree due to rounding.

How Contribution Rates Changed

The increase in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01%, therefore the proposal will not affect contribution rates in the current biennium. However, we will use the un-rounded rate increase to measure the fiscal budget changes in future biennia.

Impact on Contribution Rates: (Effective 09/01/2009)		
System/Plan	**PERS**	**SERS**
Current Members		
Employee (Plan 2)	0.000%	0.001%
Employer:		
Normal Cost	0.000%	0.001%
Plan 1 UAAL	0.000%	0.000%
Total	0.000%	0.001%

How This Impacts Budgets And Employees

Budget Impacts			
(Dollars in Millions)	**PERS**	**SERS**	**Total**
2009-2011			
General Fund	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**
2011-2013			
General Fund	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**
2009-2034			
General Fund	$0.0	$0.1	$0.1
Non-General Fund	0.0	0.0	0.0
Total State	**0.0**	**0.1**	**0.2**
Local Government	0.0	0.2	0.2
Total Employer	**0.1**	**0.3**	**0.4**
Total Employee	**$0.1**	**$0.1**	**$0.2**

Note: Totals may not agree due to rounding.

The analysis of this proposal does not consider any other proposed changes to the system. The combined effect of several changes to the systems could exceed the sum of each proposed change considered individually.

As with the costs developed in the actuarial valuation, the emerging costs of the systems will vary from those presented in the AVR or this draft fiscal note to the extent that actual experience differs from the actuarial assumptions.

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

To determine the sensitivity of the actuarial results to the best-estimate assumptions or methods selected for this pricing we varied the following assumption:

- The number of members who will receive the increased benefits.

Currently this proposal provides increased benefits to active members who earn service after the effective date of this proposal and before the end of the 2010 school year. We priced this proposal assuming all 132 current active members will receive the service credit. However, the actual number of members may differ. Current active members may choose to retire or terminate from active service before they become eligible to receive the increase in service credit, and current vested terminated members may choose to return to work and would then qualify to receive the increase in service credit. A decrease in the number of members eligible to receive this service credit would decrease the liabilities and associated budget costs compared to the proposal.

The following tables show the impact if:
- Current active members receive the increase in service as assumed (“Proposal”).
- Current active and vested terminated members receive the increase in service (“All”).

Members Impacted		
All Systems	**Proposal**	**All**
Number of Members Affected	132	192
Increase in Service (Years)	37.84	57.09

Impact on Pension Liability - All Systems		
(Dollars in Millions)	**Proposal**	**All**
Today's Value of All Future Pensions	$0.2	$0.3
Earned Pensions Not Covered by Today's Assets	$0.0	$0.0

Budget Impacts - All Systems		
(Dollars in Millions)	**Proposal**	**All**
2009-2011		
General Fund - State	$0.0	$0.0
Total Employer	0.0	0.0
2011-2013		
General Fund - State	0.0	0.0
Total Employer	0.0	0.0
2009-2034		
General Fund - State	0.1	0.2
Total Employer	$0.4	$0.5

ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost methods are appropriate for the purposes of this pricing exercise.
2. The actuarial assumptions used are appropriate for the purposes of this pricing exercise.
3. This draft fiscal note is based upon data provided by the Department of Retirement Systems (DRS). An audit of the data was not performed. I relied on the data provided as complete and accurate for the purposes of this pricing exercise.
4. Use of another set of methods, assumptions, and data may also be reasonable, and might produce different results.
5. This draft fiscal note has been prepared for the Select Committee on Pension Policy.
6. This draft fiscal note has been prepared, and opinions given, in accordance with Washington State law and accepted actuarial standards of practice as of the date shown on page 1 of this draft fiscal note.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. While this draft fiscal note is meant to be complete, the undersigned is available to provide extra advice and explanations as needed.

Matthew M. Smith, FCA, EA, MAAA
State Actuary

APPENDIX A – SPECIAL DATA NEEDED

DRS provided the unaudited data for this proposal. The data contained 212 records, with the current service credited under the old rules and the new service credited based on DRS' understanding and application of this proposal. The difference between the new service credited and the current service credited equals the additional service amount the member would receive under this proposal.

We matched the records provided with our valuation file. Only 192 of the 212 records are active (132) or terminated vested (60) members of the retirement system as of our last valuation, June 30, 2007. For each matched record, we increased their total service by the additional service amount provided by DRS.

The following table summarizes the active member data we used for this proposal.

	PERS 2/3			SERS 2/3		
Year of Hire	**Number of Members**	**Total Additional Service**	**Average Additional Service**	**Number of Members**	**Total Additional Service**	**Average Additional Service**
1977	1	0.08	0.08	1	0.33	0.33
1978	4	1.17	0.29	19	10.08	0.53
1979	2	0.33	0.17	31	8.08	0.26
1980	4	0.92	0.23	16	5.17	0.32
1981	1	0.08	0.08	9	2.17	0.24
1982	1	0.25	0.25	12	2.67	0.22
1983	2	0.42	0.21	14	2.67	0.19
1984	2	0.58	0.29	5	1.08	0.22
1985	1	0.17	0.17	5	0.92	0.18
1986	1	0.17	0.17	0	0.00	0.00
1987	1	0.50	0.50	0	0.00	0.00
Total	**20**	**4.67**	**0.23**	**112**	**33.17**	**0.30**

Otherwise, we developed these costs using the same assets and data as disclosed in the Actuarial Valuation Report (AVR).

GLOSSARY OF ACTUARIAL TERMS

Actuarial Accrued Liability: Computed differently under different funding methods, the actuarial accrued liability generally represents the portion of the present value of fully projected benefits attributable to service credit that has been earned (or accrued) as of the valuation date.

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of actuarial assumptions (i.e. interest rate, rate of salary increases, mortality, etc.).

Aggregate Funding Method: The Aggregate Funding Method is a standard actuarial funding method. The annual cost of benefits under the Aggregate Method is equal to the normal cost. The method does not produce an unfunded liability. The normal cost is determined for the entire group rather than on an individual basis.

Entry Age Normal Cost Method (EANC): The EANC method is a standard actuarial funding method. The annual cost of benefits under EANC is comprised of two components:

- Normal cost.
- Amortization of the unfunded liability.

The normal cost is determined on an individual basis, from a member's age at plan entry, and is designed to be a level percentage of pay throughout a member's career.

Normal Cost: Computed differently under different funding methods, the normal cost generally represents the portion of the cost of projected benefits allocated to the current plan year.

Projected Unit Credit (PUC) Liability: The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date (past service).

Projected Benefits: Pension benefit amounts which are expected to be paid in the future taking into account such items as the effect of advancement in age as well as past and anticipated future compensation and service credits.

Unfunded PUC Liability: The excess, if any, of the Present Value of Benefits calculated under the PUC cost method over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.

Unfunded Actuarial Accrued Liability (UAAL): The excess, if any, of the actuarial accrued liability over the actuarial value of assets. In other words, the present value of benefits earned to date that are not covered by plan assets.

The Select Committee on Pension Policy

SERS Past Part-Time Service Credit

Darren Painter, Policy Analyst
November 18, 2008

Office of the State Actuary
"Securing tomorrow's pensions today."

What Is The Issue?

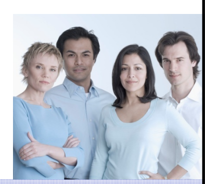
- In the past, some members made contributions without receiving service credit
  - Occurred under prior service credit rules
  - Current rules generally don't allow "non-credited" service
- SERS members want credit for this past service
- Other approaches

Committee Activity

- Briefings in June & October
- Executive Committee recommendation
- Opportunity for formal action today

Policy Highlights

- Impacts all the state's major retirement systems
- The Legislature has addressed this issue before
  - Rules changed going forward (1991)
  - Not retroactive except for some teachers
- Differs from other retroactive benefit increases

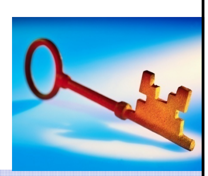


Options For Addressing Non-credited Service

- Refund contributions
- Apply current rules
  - to all past service
  - to past educational service
- Apply current half-time rules to past educational service

Two Key Policy Decisions

- How is the issue viewed?
  - Contribution issue or service credit issue
  - Refunds vs. crediting service
- Who is primarily impacted?
  - School employees or all employees



Executive Committee Recommendation

- Policy view
  - Service credit issue
  - School employees
- Apply current half-time rules to past educational service
  - Grant half-time service credit to members who worked at least half-time for an educational employer
  - Requires limited retroactive policy change
  - Consistent with earlier change for teachers
  - Impacts about 130 members
- Bill draft and fiscal note in materials

Preliminary Total Employer Rate Increase

System	Option 1 Refund	Option 2A Apply Current Rules: All	Option 2B Apply Current Rules: School	Option 3** Apply Half-Time Rules
PERS	*	*	*	*
TRS	*	.01%	.01%	n/a
SERS	*	.01%	.01%	*
PSERS	*	*	n/a	n/a
LEOFF	*	*	n/a	n/a
WSPRS	*	n/a	n/a	n/a

n/a: Option does not apply to system.
**Insufficient to immediately impact rates.*
***Executive Committee recommendation.*

Preliminary Fiscal Costs

($ in Millions)	Option 1 Refund	Option 2A Apply Current Rules: All	Option 2B Apply Current Rules: School	Option 3* Apply Half-Time Rules
2009-2011				
Total GFS	$0.0	$0.7	$0.7	$0.0
Total Employer	0.0	1.1	1.1	0.0
25-Year				
Total GFS	1.4	7.6	6.2	0.1
Total Employer	$3.8	$18.6	$11.0	$0.4

**Executive Committee recommendation.*

Possible Next Steps

- Recommend the Executive Committee's bill to Legislature
- Take some other action
- Take no action

10. $150,000 Death Benefit

$150,000 Death Benefit

Description of Issue

The retirement systems provide a $150,000 death benefit for public employees who die as a result of a duty-related injury or illness. The benefit amount has not changed since the benefit was first established in 1996. Stakeholders are asking the SCPP to revisit adjusting the amount for inflation.

Actuaries expect fewer than 13 duty-deaths each year from a group of over 290,000 public employees.

This issue raises two basic policy questions. Is the current amount of the death benefit sufficient, or should it be increased for past inflation? Should the death benefit be protected against future inflation?

Policy Highlights

- The relative value of the death benefit has declined 27 percent due to past inflation.
- COLAs for lump sums provide equity across generations—not inflation protection for an individual's income.
- Some policy makers may prefer an insurance approach rather than a COLA approach.
- Automatic and ad-hoc COLAs can be equally effective in maintaining the value of benefits—with different implications for control.
- The Legislature has previously rejected automatic COLAs for the death benefit.
- The SCPP recommended legislation on this issue in 2007 and 2008.

Committee Activity

Staff briefed the full committee on three options at the October meeting. Following the meeting, the Chair requested staff to prepare draft legislation and pricing for an additional option of increasing the benefit to $175,000. Staff will brief the full committee on this option at the November meeting.

Options for Adjusting the Duty-Death Benefit

Policy makers who feel the current death benefit should be adjusted for inflation may consider the following options:

- **Provide a One-Time Adjustment for Past Inflation.**
  - Restores the relative value of the benefit to its original level.
  - Doesn't prevent future loss in value due to inflation.

- **Provide an Automatic CPI-Based COLA.**
  - Doesn't recover value already lost due to inflation.
  - Generally prevents further loss of value due to inflation.
  - Requires policy makers to give up some control over the benefit, but may reduce the need to revisit this in the future.

- **One-Time Adjustment Plus Automatic COLA.**
  - Recovers past value and generally prevents future loss of value.
  - Requires policy makers to give up some control over the benefit, but may reduce the need to revisit in the future.

- **Increase to $175,000.**
  - Recovers some value lost due to past inflation.
  - Doesn't prevent future loss in value due to inflation.

Next Steps

Public hearing with possible executive action.

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In Brief

ISSUE

The retirement systems provide a $150,000 death benefit for public employees who die as a result of a duty-related injury or illness. The benefit amount has not changed since 1996.

The LEOFF 2 Board asked the SCPP to consider adjusting the amount of this benefit for past inflation and adding an automatic COLA to address future inflation.

The SCPP twice recommended legislation that would have applied an automatic COLA to the death benefit. The COLA provisions did not pass the Legislature.

MEMBER IMPACT

*Actuaries expect fewer than 13 duty-deaths each year from a group of over 290,000 public employees.**

**As of June 30, 2007.*

Darren Painter
Policy Analyst
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painter.darren@leg.wa.gov

$150,000 Death Benefit

Current Situation

The retirement systems provide a $150,000 lump sum (or one-time) death benefit for public employees who die as a result of a duty-related injury or illness. The benefit amount is set in statute and has not changed since the benefit was first established in 1996. The benefit is not subject to federal income tax.

The benefit is available to members of all state retirement systems*. Determination of eligibility is made by the Department of Labor and Industries (L&I).

The Law Enforcement Officers' and Fire Fighters' Plan 2 Retirement Board (LEOFF 2 Board) asked the SCPP to consider adjusting the amount of this benefit for past inflation and adding an automatic COLA to address future inflation.

**Also state, school district, and higher education employees who are not members of a state retirement system; paid from the state general fund.*

History

History of the $150,000 Death Benefit

The $150,000 death benefit was first established in the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) and the Washington State Patrol Retirement System (WSPRS) in 1996. The benefit was subsequently extended to various other groups of public employees over a period of several years. See **Appendix A** for a legislative history of the benefit.

Fifty-four $150,000 death benefits have been paid out since the benefit was first established—the majority being paid for LEOFF members (see **Figure 1**).

Figure 1

Number of $150,000 Death Benefits Paid*	
System	Benefits Paid
LEOFF	32
PERS	14
VFF	2
TRS	1
SERS	1
WSPRS	1
Unknown (paid from general fund)	3
Total	**54**

**As of 9/25/2008. Length of reporting period varies among systems.*

SCPP has Recommended Death Benefit Bills

The SCPP studied this issue in coordination with the LEOFF 2 Board in 2006 and 2007. The committee recommended legislation in the 2007 and 2008 sessions that would have applied an automatic cost-of-living-adjustment (COLA) to the death benefit. The COLA provisions did not pass the Legislature. See below for more details concerning the SCPP legislation.

The Legislature has Rejected Death Benefit COLAs

Bills with provisions that would have automatically increased the amount of the $150,000 death benefit for inflation were introduced in the past three legislative sessions. None of the bills passed the Legislature with the COLA provisions intact.

Bills that would have automatically increased the amount of the $150,000 death benefit for inflation were introduced in the past three legislative sessions.

2006 Session

HB 2933/SB 6724 dealt with the death benefit for LEOFF Plan 2. The bill expanded eligibility and provided an automatic COLA on the benefit amount. The proposed COLA would have annually increased the amount of the death benefit based on cumulative changes in the Consumer Price Index for Wage Earners and Clerical Workers for Seattle-Tacoma-Bremerton (CPI-W, STB), up to a maximum of 3 percent per year. This is the same increase provided for pensions in the Plans 2/3 retirement systems. The COLA was removed before the bill passed the Legislature.

2007 Session

HB 1266/SB 5177, an SCPP bill, made similar changes to the death benefit as the 2006 bill except it applied to all plans. The COLA was removed from the House bill in the Appropriations Committee, but was retained in the Senate version of the bill that passed Ways and Means. The House version of the bill, without the COLA, ultimately passed the Legislature.

2008 Session

HB 3026/SB 6664, another SCPP bill, contained the same COLA provisions as introduced in the earlier legislation. The bill was heard in the Senate Ways and Means Committee and received no hearing in the House.

Comparisons

Other Death Benefits Provided

The $150,000 death benefit is one of many death benefits that are provided for members*. Others include:

Many death benefits are provided for members.

- ❖ Survivor and death benefits from the retirement plan.
- ❖ L&I death benefits.
- ❖ Social Security survivor benefits.
- ❖ Federal public safety officers death benefits.
- ❖ Reimbursement of premiums paid to the Health Care Authority.

A detailed list of the various death benefits provided is contained in **Appendix B**. Among these, the most significant other lump sum death benefit provided is the federal Public Safety Officers' Benefits Death Benefit. This benefit ($315,746 in 2008) is payable to survivors of law enforcement officers, fire fighters, and other public safety personnel who die in the line of duty. The benefit is annually adjusted for inflation.

**Employer provided life insurance is beyond the scope of this paper and is not considered among the death benefits provided.*

Death Benefits in Comparative Systems

Most of Washington's comparative systems provide survivor annuities similar to those in Washington's retirement systems. The annuities are generally based on the member's earned benefit or some percentage of the member's salary.

Five of Washington's comparative systems also provide some type of lump sum death benefit (see **Figure 2**). The three systems (California, Idaho, and Iowa) that provide fixed-dollar lump sum benefits similar to Washington do not automatically increase the benefit amount for inflation. Three systems (Colorado, Idaho, and Wisconsin) provide a lump sum based on the member's contributions. Since contributions are based on salaries, and salaries grow with inflation, contribution-based lump sums effectively have built-in inflation adjustments. One system (California) provides a lump sum that is "periodically adjusted." Idaho and Iowa provide an enhanced return of contributions and a special duty-related lump sum death benefit for public safety employees.

Figure 2

Lump Sum Death Benefits in Comparative Systems*

System	Benefit Amount	COLA
California CALSTRS	$24,652	Periodically adjusted.
Colorado PERA	200% Return Of Contributions plus interest (ROC).	None.
Idaho PERSI	200% ROC. Also $100,000 for police and firefighters killed in line of duty.	None.
Iowa IPERS	100% ROC plus additional amount based on salary and service. Also $100,000 for public safety officer killed in line of duty.	None.
Wisconsin WRS	200% ROC.	None.

**Source: Member handbooks published on system administrator's web sites as of 10/08/2008.*

Policy Analysis

This Issue Raises Two Basic Policy Questions

The issue of whether or not to adjust the $150,000 death benefit for inflation raises two basic policy questions:

- Is the current amount of the death benefit sufficient, or should it be increased for past inflation?
- Should the death benefit be protected against future inflation?

The way policy makers respond will likely depend upon three key factors.

The way policy makers respond to these questions will likely depend upon three key factors:

- How they choose to apply policy on inflation protection to the death benefit.
- How they view the purpose of the death benefit.
- How much control they wish to keep over the death benefit.

The rest of this paper will explore these and other factors that policy makers may consider in addressing this issue.

Inflation Erodes the Relative Value of the Death Benefit

The value of the death benefit has declined 27 percent since 1996.

Inflation erodes the relative value of a fixed dollar amount over time. The $150,000 death benefit was first established in 1996. The cumulative effect of inflation since then has eroded 27 percent* of the relative value of the benefit. Put another way, the amount of the death benefit would need to be increased to $205,000 to provide the same level of purchasing power that it did in1996. Absent any adjustment, inflation will continue to erode the value of the death benefit in the future.

**Based on the Consumer Price Index for Urban Wage Earners and Clerical Workers for Seattle-Tacoma-Bremerton (CPI-W, STB), all Items.*

The State's Policy on Inflation Protection for Pensions

State policy on protecting retirement benefits from inflation can be found in existing policy statements and further inferred from plan design. The SCPP has adopted as a stated goal "... to increase and maintain the purchasing power of retiree benefits in the Plans 1 of PERS and TRS. . . ." The Plans 2/3 of the state's retirement systems, the most recently created tiers, provide an annual COLA on retirement pensions. The Plans 2/3 COLA is based on inflation as measured by changes in a Consumer Price Index (CPI). The inclusion of this COLA in the Plans 2/3 design indicates a clear desire to protect retirement pensions from the effects of inflation.

Policies on inflation protection were not necessarily designed for lump sum benefits.

These policies around inflation protection were designed to apply to ongoing *pension* benefits and not necessarily one-time *lump sum* benefits. Policy makers may wish to consider to what extent, if any, inflation protection policies apply to non-pension benefits like the $150,000 death benefit.

COLAs for Pensions and Lump Sums have Different Policy Implications

Why would the nature of the benefit matter when considering inflation protection policies? COLAs for ongoing pensions have different policy implications than COLAs for one-time lump sum benefits. One provides inflation protection, while the other provides equity across generations.

Providing a COLA for a pension or other annuity-type benefit provides inflation protection for an *individual's* income. The COLA helps maintain the relative value of the pension payments over time by offsetting the effects of inflation.

COLAs for lump sums maintain value among generations.

In contrast, providing a COLA for a lump sum benefit maintains the value of the benefit among successive *generations* of recipients. It ensures that later recipients are able to purchase the same amount of goods and services with the benefit that earlier recipients could. It does not provide inflation protection for an individual's income. Why not? A lump sum payment is only received once. It doesn't become part of the recipient's ongoing income stream and consequently doesn't lose its value (from the recipient's perspective) over time.

Lump Sum Death Benefits are Less Likely to have COLAs

Given the different policy implications of COLAs for annuities and lump sums, policy makers may wish to consider current practice in this area. **Figure 3** shows that death benefits for retirement system members paid in the form of a monthly annuity are more likely to have inflation protection than benefits paid in a lump sum. A detailed list of the various death benefits provided is contained in **Appendix B**.

Figure 3

Death Benefits Provided*			
Type	**Total**	**COLA**	**%COLA**
Annuity	9	7	78%
Lump Sum	7	3	43%

**Similar benefits in state retirement systems are considered a single type.*

In the preceding figure, the "Total" column shows the total number of benefits of each type (annuity or lump sum); the "COLA" column shows how many include an automatic COLA; and the "%COLA" column shows the percentage of annuity and lump sum benefits with an automatic COLA.

The Death Benefit is Designed to Provide Temporary Assistance

A key policy consideration is the intended purpose of the benefit.

Policy makers may consider the purpose of the $150,000 death benefit in determining how to apply policy on inflation protection. Is the benefit intended to replace income and support an ongoing standard of living? Or, is the benefit intended to provide one-time relief for specific situations? The answers to these questions have implications for policy decisions.

The death benefit is a one-time payment that is not related to a member's salary. Recipients may do with the payment whatever they wish—including spending the entire amount at once. Given this design, it is unlikely that the benefit was intended to replace income and support an ongoing standard of living. Rather, it is more likely that the death benefit was primarily intended to provide temporary financial assistance following the death of a member.

The purpose of the benefit may affect how policy makers view this issue. From the perspective of policy makers, there may be less need to adjust for inflation a benefit that is transitional and does not serve to replace income or maintain an ongoing standard of living.

Policy Makers may take an Insurance-Based Approach

The death benefit more closely resembles an insurance benefit than a pension.

The design and purpose of the $150,000 death benefit more closely resembles an insurance benefit than a traditional pension benefit. It is a one-time payment of a fixed-dollar amount that provides temporary financial assistance—much like term life insurance. Policy makers who view this as an insurance-type benefit may be inclined to take more of an insurance-based approach to this issue. An insurance approach would involve periodically reviewing the "policy" and adjusting the coverage amount based on the risks and needs at that time. Under this approach, the policy focus shifts away from COLAs and more towards the adequacy of the benefit provided.

Assessing the Adequacy of the Death Benefit may be Challenging

Policy makers may find it challenging to assess the adequacy of a benefit (like the $150,000 death benefit) that is not dedicated to a specific purpose. Since the value of the benefit can't easily be measured against a specific outcome, assessments of adequacy will likely be highly subjective. Such assessments may involve considering how the $150,000 death benefit fits in with all the other death benefits provided—many of which are pension benefits that do have inflation protection. This could be a complex task given the number and variety of different death benefits provided, and the fact that survivors may qualify for multiple death benefits (see **Appendix B**).

Policy makers may assume the amount was adequate when the benefit was first enacted.

For the sake of simplicity, some policy makers may assume the amount was adequate when the benefit was first enacted in 1996. Under this assumption, all that is needed to ensure the adequacy of the benefit today is to adjust the amount of the benefit for past inflation.

Duty-Related Death Benefits may Impact Recruitment

When contemplating adjustments to the $150,000 death benefit, policy makers may also consider the purpose and adequacy of the benefit from an employer perspective. Duty-related death benefits may impact the ability of employers to recruit for high-risk occupations. The availability and generosity of such benefits may serve as an added inducement for employees considering such occupations. This would likely have the greatest impact for public safety employers. The fact that the $150,000 death benefit was first established for police and fire fighters (see **History**) may be indicative of a greater interest in duty-related death benefits by public safety groups.

Automatic and Ad-Hoc COLAs can be Equally Effective in Maintaining the Value of Benefits

Policy makers who feel the $150,000 death benefit should be adjusted for inflation will likely consider how to adjust it. Most likely, this will involve some form of a COLA—since COLAs are a common and effective way to adjust benefits for inflation. There are two basic approaches to COLAs that policy makers may wish to consider: ad-hoc and automatic. The approach chosen has implications for how much control policy makers retain over the benefit.

Policy makers who want the most control will likely prefer an ad-hoc approach.

Ad-hoc COLAs are one-time increases. Ad-hoc COLAs are generally more backward-looking. They can be very effective at making up for past inflation, but usually do little to address future inflation. Ad-hoc COLAs can give policy makers the most flexibility in reacting to specific situations and in controlling costs. Policy makers who want to maintain the most control in adjusting benefits will likely prefer an ad-hoc approach.

Policy makers who want less involvement will likely prefer an automatic approach.

In contrast, automatic COLAs are ongoing increases and tend to be more forward-looking. Automatic COLAs can be very effective at protecting benefits against future inflation, but may do little to address lost purchasing power due to past inflation. Automatic COLAs may be preferred from the member viewpoint since they are ongoing and don't require continual action by policy makers. However, for the same reasons, it may be more difficult to fine-tune an automatic COLA for a specific situation. Policy makers who want less involvement in the process of adjusting benefits will likely prefer an automatic approach.

A common way of implementing automatic COLAs is to base the COLA on a measure of inflation such as the CPI. This process of linking a benefit to an underlying measure of inflation is known as *indexing*. Indexing is a direct and effective way to protect benefits against inflation. This is the method chosen by the SCPP in prior years when the committee recommended applying an automatic COLA to the death benefit (see **History**). **Appendix C** contains a more complete discussion on the various ways to index a benefit.

Periodically granting ad-hoc COLAs can have much the same effect as an automatic COLA.

Ad-hoc COLAs can be as effective in maintaining the value of a benefit as automatic COLAs, depending on how they are administered. Periodically granting ad-hoc COLAs to make up for past inflation can have much the same effect as providing an automatic COLA. The main difference is that ad-hoc COLAs may occur less frequently than every year. When this happens, the benefit loses more value in the years between ad-hoc COLAs than it would lose under an automatic COLA. Given that both approaches can be equally effective in maintaining value, the approach taken will likely depend on how much control and involvement policy makers want in the process of adjusting benefits.

Conclusion

The issue of adjusting the $150,000 death benefit for inflation raises two basic policy questions. Is the current amount sufficient or should it be increased for past inflation? Should it be protected against future inflation?

How policy makers respond to these questions will likely depend upon three key factors:

- How they choose to apply policy on inflation protection to the death benefit.
- How they view the purpose of the death benefit.
- How much control they wish to keep over the death benefit.

Some policy makers may prefer to take an insurance-based approach to this issue rather than the COLA-based approach taken in the past.

Possible Options

Policy makers who feel the current amount of the death benefit is sufficient for its intended purpose will likely be inclined to take no further action at this time. Policy makers who feel the current death benefit should be adjusted for inflation may consider one of the options below.

Preliminary pricing for each of the policy options will be available at the November meeting.

Option 1: Provide a One-Time Adjustment for Past Inflation

This option restores the relative value to its original level.

This option would grant an ad-hoc COLA on the amount of the death benefit to make up for past inflation. The amount of the death benefit would be increased to $205,000.

This option would restore the relative value of the death benefit to its original level but wouldn't prevent future loss in value due to inflation.

Option 2: Provide an Automatic CPI-Based COLA

This option generally prevents further loss of value.

This option would apply an automatic CPI-based COLA to the death benefit. The COLA would be modeled after the COLA provided for pensions in the Plans 2/3. The amount of the death benefit would annually increase based on cumulative changes in the CPI-W, STB, up to a maximum of 3 percent per year. This is the approach that has been taken by the SCPP in the past and has been rejected by the Legislature (see **History**).

This option would generally not recover value already lost due to past inflation since the annual increases are capped at 3 percent. The 3 percent cap is a cost-control feature originally intended for pension benefits. It may be of limited value for a death benefit that is paid out infrequently. This option would generally prevent further loss of value due to inflation—while long-term inflation averages 3 percent or less. This approach requires policy makers to give up some control over the benefit amount, but may reduce the need to revisit this in the future.

Option 3: One-Time Adjustment and Automatic CPI-Based COLA

This option recovers lost value and generally prevents further loss.

This option combines the previous two options. It would increase the amount of the death benefit to $205,000 and apply an automatic CPI-based COLA on the new amount.

This option would recover all value lost to past inflation as well as generally prevent further loss of value due to inflation—while long-term inflation averages 3 percent or less. This option has the same policy implications regarding the cap on the automatic COLA as discussed under Option 2. This approach also requires policy makers to give up some control over the benefit amount, but may reduce the need to revisit this in the future.

Option 4: Increase to $175,000

This option recovers some lost value.

This option would increase the amount of the death benefit to $175,000. This option would recover some of the value of the benefit lost to past inflation, but would not fully restore the benefit to its original level. This option would not prevent further loss in value due to future inflation.

Committee Activity

During their September meeting, the Executive Committee directed staff to develop policy options and bring those options back to the full committee with pricing.

Staff briefed the full committee on the first three options at the October meeting. Following the meeting, the Chair requested staff to prepare draft legislation and pricing for an additional option of increasing the benefit to $175,000. Staff will brief the full committee on this option at the November meeting.

Next Steps

Public hearing with possible executive action.

Stakeholder Input

Correspondence from:

Kelly Fox, Chair, LEOFF 2 Board, received 5/12/2008.

Bill Draft

An OSA bill draft to implement Option 4 is attached.

Draft Fiscal Note

Attached.

Appendix A: History of Legislative Changes to the $150,000 Death Benefit*

History of Legislative Changes to the $150,000 Death Benefit		
Year	**Bill**	**Effect**
1996	E2SSB 5322	$150,000 death benefit established for LEOFF and WSP.
1998	SB 5217 ESB 6305	$150,000 death benefit established in VFF. $150,000 death benefit is established for survivors of PERS 1 port and university police officers.
1999	ESSB 5180 (Budget)	$150,000 death benefit provided to teachers and paid as sundry claim from general fund. Expired 6/30/2001.
2000	EHB 2487 (Budget)	$150,000 death benefit provided to school district employees and paid as sundry claim from general fund. Expired 6/30/2001.
2001	ESSB 6153 (Budget)	$150,000 death benefit provided to state, school district, and higher education employees and paid as sundry claim from general fund. Expired 6/30/2003.
2003	HB 1207	$150,000 death benefit established in PERS, TRS, and SERS. Benefit also provided as a sundry claim to the general fund for state, school district, and higher education employees who are not eligible to receive the benefit from a state retirement system.
2006	SHB 2933	Eligibility for the $150,000 death benefit expanded to include death from duty-related illness for LEOFF 2.
2007	SHB PL 1266	Eligibility for the $150,000 death benefit expanded to include death from duty-related illness for all plans.

See **Appendix D for a description of the plan acronyms used.*

Appendix B: Death Benefit Provided for Public Employees*

Death Benefits Provided for Public Employees[1]				
Benefit	**Normal Form**	**Eligible Deaths**	**Amount**	**Annual Adjustment[2]**
LEOFF & WSP Plan 1 Survivor Pension	Annuity	Duty & Non-Duty	50%-60% of AFC	Indexed to CPI
PERS & TRS Plan 1 Survivor Benefit	Annuity or Lump Sum	Duty & Non-Duty	Member's earned benefit or return of contributions with interest (ROC)[3]	Uniform COLA on annuity -- indexed by level 3%
Plans 2/3 Survivor Benefit	Annuity or Lump Sum	Duty & Non-Duty	Member's earned benefit or ROC[3,4]	Annuity Indexed to CPI
VFF Survivor Benefit	Annuity	Duty & Non-Duty	Member's earned benefit	None -- Benefits periodically increased by Board
VFF Duty-Death Survivor Pension	Annuity	Duty	$1,589/month +$137/month per child. As of 7/1/2008.	Indexed to CPI
HIED Survivor Benefit	Annuity or Lump Sum	Duty & Non-Duty	Payout of member's account	None
LEOFF Plan 2 Survivor Health Care	Annuity	Duty	Reimbursement of premiums paid to Health Care Authority—up to $839/month for 2008	Indexed to Health Care Authority medical and dental premiums
L&I Death Benefit	Annuity	Duty	60%-70% of gross wages up to 120% of state average wage[5]	Indexed to state average wage[5]
Social Security Survivor Benefit	Annuity	Duty & Non-Duty	75%-100% of employees earned Social Security benefit	Indexed to CPI
$150,000 Death Benefit	Lump Sum	Duty	$150,000 (+$2,000 in VFF)	None
VFF Funeral Benefit	Lump Sum	Duty	$2,000	None
TRS 1 Death Benefit	Lump Sum	Duty & Non-Duty	$400 or $600	None
L&I Death Lump Sum	Lump Sum	Duty	100% state average monthly wage[5]	Indexed to state average wage[5]
L&I Burial Benefit	Lump Sum	Duty	Up to 200% state average monthly wage[5]	Indexed to state average wage[5]
Social Security Burial Benefit	Lump Sum	Duty & Non-Duty	$255	None
Federal Public Safety Officers' Death Benefit	Lump Sum	Duty	$315,746 as of 10/01/2008	Indexed to CPI

1. Eligibility varies by group. Some benefits are not available to all groups and some groups may be eligible for multiple benefits. Excludes employer provided life insurance.

2. Excludes optional COLAs purchased by recipient.

3. Actuarial reduction applied if death is not duty-related.

4. 150% ROC for LEOFF Plan 2; payout of member's DC account for Plans 3.

5. $3,727 as of 7/01/2008.

See **Appendix D for a description of the plan acronyms used.*

Appendix C: Indexing Benefits

A frequently used method of protecting the value of a benefit against inflation is indexing. Indexing involves making annual adjustments to the benefit amount based on changes in an underlying measure of inflation.

One of the most commonly used measures of inflation is the Consumer Price Index (CPI). The CPI records changes in the price of a set "market basket" of goods and services at different points in time. The U.S. Department of Labor publishes numerous indexes that measure inflation based on different market baskets and geographic regions. Each CPI produces a slightly different measure of inflation. The CPI most commonly used in Washington State's retirement systems is the Consumer Price Index for Urban Wage Earners and Clerical Workers for Seattle-Tacoma-Bremerton (CPI-W, STB). An individual may experience inflation quite different from that measured by the CPI if the goods and services purchased by the individual do not closely match the market basket used by the CPI.

A key issue in indexing benefits is the amount of inflation protection to provide. The value of a benefit may be:

- Fully protected from inflation (full indexing).
- Protected up to a maximum amount of inflation (partial indexing).
- Protected against a set amount of inflation (level indexing).

A **fully indexed** benefit increases at the same percentage change as inflation each year. This method ensures the full purchasing power of the benefit is always maintained, but can lead to greater than expected costs if actual inflation exceeds the amount assumed for funding the benefit. Examples of fully indexed retirement benefits include Social Security, which is indexed to the CPI-W, All U.S. Cities; and the LEOFF Plan 1 pension, which is indexed to the CPI-W, STB.

A **partially indexed** benefit increases with the percentage change in inflation each year up to a maximum percentage. In years where inflation exceeds the maximum, the benefit will lose some purchasing power.

The index can be designed to allow the benefit to recover lost purchasing power during periods when actual inflation is lower than the maximum. This method can maintain most of the purchasing power of a benefit while controlling costs and promoting stable funding. Examples of partially indexed retirement benefits are Plans 2/3 pensions, which are indexed to the CPI-W, STB, to a maximum of 3 percent.

A **level indexed** benefit increases by a fixed percentage every year. Purchasing power is lost in years when inflation exceeds the fixed percentage and is gained in years when inflation is less than the fixed percentage. This method is simple to administer and can maintain most of the purchasing power of a benefit while controlling costs and promoting stable funding. Under this method, if actual inflation is consistently less than the fixed amount, the purchasing power of the benefit will increase. An example of a level indexed retirement benefit is the PERS and TRS Plan 1 Uniform COLA, which increases by 3 percent each year.

Appendix D: Plan Acronyms

- Public Employees' Retirement System (PERS)
- Teachers' Retirement System (TRS)
- School Employees' Retirement System (SERS)
- Public Safety Employees' Retirement System (PSERS)
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF)
- Washington State Patrol Retirement System (WSPRS)
- Volunteer Fire Fighters' and Reserve Officers' Relief and Pension Fund (VFF)
- Judicial Retirement System (JRS)
- Higher Education Retirement Plans (HIED)

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STATE OF WASHINGTON

LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS' PLAN 2 RETIREMENT BOARD

P.O. Box 40918 • Olympia, Washington 98504-0918 • (360) 586-2320 • FAX (360) 586-2329 • www.leoff.wa.gov

May 12, 2008

Select Committee on Pension Policy
C/O The Office of the State Actuary
Post Office Box 40914
Olympia, Washington 98504-0914

Dear Honorable Members of the Select Committee on Pension Policy:

On behalf of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Retirement Board (Board), I would like to thank you for the cooperative working relationship we have shared in the past and look forward to a similar partnership in the future.

I would like to bring several topics back to your attention as you begin preparation for the 2008 interim. It is our hope that the Select Committee on Pension Policy (SCPP) and the Board can work cooperatively on these issues to once again develop legislation. I have provided a brief summary of each topic for your reference:

Interruptive Military Service Credit

Working cooperatively last interim, the Board and the SCPP jointly endorsed a bill that would have eliminated a member's obligation to pay for interruptive military service credit if the member served during a period of war. The Board is once again interested in working cooperatively with the SCPP on the issue and feels the following additional question will need to be further explored:

- Should the benefit apply to all periods of interruptive military service which have not yet been recovered?

Inflationary Adjustment for $150,000 Death Benefit

The Board is interested in once again working with the SCPP to further study the effect of adding an inflationary adjustment to all the state retirement plans that provide the $150,000 death benefit. In addition to last year's study the Board feels following issues will need to be explored further:

- Should an adjustment in the lump sum amount be made to account for inflation since the creation of the benefit?

- Should both the lump sum adjustment and the addition of the inflationary adjustment be included in the bill?

Military Service Death Benefit

The Board and the SCPP jointly recommended legislation to the 2008 Legislature, which would have provided an unreduced annuity to qualifying survivors of members of all plans, who leave employment due to service in the National Guard or Reserves and die while in military service, during a period of war. The Board would like to continue our joint work to eliminate the "early retirement" actuarial reduction applied to the pensions of members who die while honorably serving our country.

Fish and Wildlife Enforcement Officer Service Credit Transfer

The Board and the SCPP also jointly recommended legislation last session that would have permitted Department of Fish and Wildlife Enforcement Officers to transfer service credit earned in the Public Employees' Retirement System (PERS) Plan 2 as enforcement officers into the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 2. The Board feels the following issue may need to be further explored as well:

- Should PERS 3 members be included in the transfer group?

Please feel free to contact me or Steve Nelsen, LEOFF 2 Board Executive Director, should you have any questions or like any additional information. Steve can be reached at (360) 586-2320 or steve.nelsen@leoff.wa.gov, and I can be contacted at (360) 943-3030 or pres@wscff.org.

We would be happy to meet with you to discuss these topics at an upcoming SCPP or LEOFF Plan 2 Retirement Board meeting. Thank you for your consideration and we look forward to working with you.

Sincerely,

Kelly L Fox

Kelly Fox, Chair

cc: Matt Smith, State Actuary

Darren Painter 786-6155
OSA
November 4, 2008 (12:14 PM)

AN ACT Relating to increasing the duty-related death benefit for public employees to $175,000; amending RCW 41.04.017, 41.24.160, 41.26.048, 41.32.053, 41.35.115, 41.37.110, 41.40.0931, 41.40.0932, 43.43.285; and declaring an emergency.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

Sec. 1. RCW 41.04.017 and 2007 c 487 s 1 are each amended to read as follows:

A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid as a sundry claim to the estate of an employee of any state agency, the common school system of the state, or institution of higher education who dies as a result of (1) injuries sustained in the course of employment; or (2) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter, and is not otherwise provided a death benefit through coverage under their enrolled retirement system under chapter 402, Laws of 2003. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the director of the department of general administration by order under RCW 51.52.050.

Sec. 2. RCW 41.24.160 and 2001 c 134 s 2 are each amended to read as follows:

(1)(a) Whenever a participant dies as the result of injuries received, or sickness contracted in consequence or as the result of the performance of his or her duties, the board of trustees shall order and direct the payment from the principal fund of (i) the sum of one hundred ((~~fifty-two~~)) <u>seventy-seven</u> thousand dollars to his widow or her widower, or if there is no widow or widower, then to his or her dependent child or children, or if there is no dependent child or children, then to his or her dependent parents or either of them, or if there are no dependent parents or parent, then the death benefit shall be paid to the member's estate, and (ii)(A) the sum of one thousand two hundred seventy-five dollars per month to his widow or her widower during his or her life together with the additional monthly sum of one hundred ten dollars for each child of the member, unemancipated or under eighteen years of age, dependent upon the member for support at the time of his or her death, (B) to a maximum total of two thousand five hundred fifty dollars per month.

(b) Beginning on July 1, 2001, and each July 1st thereafter, the compensation amount specified in (a)(ii)(B) of this subsection shall be readjusted to reflect the percentage change in the consumer price index, calculated as follows: The index for the calendar year preceding the year in which the July calculation is made, to be known as "calendar year A," is divided by the index for the calendar year preceding calendar year A, and the resulting ratio is multiplied by the compensation amount in effect on June 30th immediately preceding the July 1st on which the respective calculation is made. For the purposes of this subsection, "index" means the same as the definition in RCW 2.12.037(1).

(2) If the widow or widower does not have legal custody of one or more dependent children of the deceased participant or if, after the death of the participant, legal custody of such child or children passes from the widow or widower to another person, any payment on account of such child or children not in the legal custody of the widow or widower shall be made to the person or persons having legal custody of such child or children. Such payments on account of such child or children shall be subtracted from the amount to which such widow or widower would have been entitled had such widow or widower had legal custody of all the children and the widow or widower shall receive the remainder after such payments on account of such child or children have been subtracted. If there is no widow or widower, or the widow or widower dies while there are children, unemancipated or under eighteen years of age, then the amount of one thousand two hundred seventy-five dollars per month shall be paid for the youngest or only child together with an additional one hundred ten dollars per month for each additional of such children to a maximum of two thousand five hundred fifty dollars per month until they become emancipated or reach the age of eighteen years; and if there are no widow or widower, child, or children entitled thereto, then to his or her parents or either of them the sum of one thousand two hundred seventy-five dollars per month for life, if it is proved to the satisfaction of the board that the parents, or either of them, were dependent on the deceased for their support at the time of his or her death. In any instance in subsections (1) and (2) of this section, if the widow or widower, child or children, or the parents, or either of them, marries while receiving such pension the person so marrying shall thereafter receive no further pension from the fund.

(3) In the case provided for in this section, the monthly payment provided may be converted in whole or in part into a lump sum payment, not in any case to exceed twelve thousand dollars, equal or proportionate, as the case may be, to the actuarial equivalent of the monthly payment in which event the monthly payments shall cease in whole or in part accordingly or proportionately. Such conversion may

be made either upon written application to the state board and shall rest in the discretion of the state board; or the state board is authorized to make, and authority is given it to make, on its own motion, lump sum payments, equal or proportionate, as the case may be, to the value of the annuity then remaining in full satisfaction of claims due to dependents. Within the rule under this subsection the amount and value of the lump sum payment may be agreed upon between the applicant and the state board.

Sec. 3. RCW 41.26.048 and 2007 c 487 s 2 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's death benefit shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2) The benefit under this section shall be paid only when death occurs: (a) As a result of injuries sustained in the course of employment; or (b) as a result of an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 4. RCW 41.32.053 and 2007 c 487 s 3 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member has nominated by written

designation duly executed and filed with the department. If no such designated person or persons are still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) The benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 5. RCW 41.35.115 and 2007 c 487 s 4 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member has nominated by written designation duly executed and filed with the department. If no such designated person or persons are still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) The benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 6. RCW 41.37.110 and 2007 c 487 s 5 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) <u>seventy-five</u> thousand dollar death benefit shall be paid to the member's estate, or the person or persons, trust, or organization the member has nominated by written designation duly executed and filed with the department. If the designated person or persons are not still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) The benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 7. RCW 41.40.0931 and 2007 c 487 s 6 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) <u>seventy-five</u> thousand dollar death benefit for members who had the opportunity to transfer to the law enforcement officers' and firefighters' retirement system pursuant to chapter 502, Laws of 1993, but elected to remain in the public employees' retirement system, shall be paid to the member's estate, or such person or persons, trust, or organization as the member has nominated by written designation duly executed and filed with the department. If there is no designated person or persons still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) Subject to subsection (3) of this section, the benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment as a general authority police officer; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

(3) The benefit under this section shall not be paid in the event the member was in the act of committing a felony when the fatal injuries were suffered.

Sec. 8. RCW 41.40.0932 and 2007 c 487 s 7 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member has nominated by written designation duly executed and filed with the department. If no such designated person or persons are still living at the time of the member's death, the member's death benefit shall be paid to the member's surviving spouse as if in fact the spouse had been nominated by written designation, or if there is no surviving spouse, then to the member's legal representatives.

(2) The benefit under this section shall be paid only where death occurs as a result of (a) injuries sustained in the course of employment; or (b) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

Sec. 9. RCW 43.43.285 and 2007 c 488 s 1 are each amended to read as follows:

(1) A one hundred ((~~fifty~~)) seventy-five thousand dollar death benefit shall be paid to the member's estate, or such person or persons, trust or organization as the member shall have nominated by written designation duly executed and filed with the department. If there be no such designated person or persons still living at the time of the member's death, such member's death benefit shall be paid to the member's surviving spouse as if in fact such spouse had been nominated by written designation, or if there be no such surviving spouse, then to such member's legal representatives.

(2)(a) The benefit under this section shall be paid only where death occurs as a result of (i) injuries sustained in the course of employment; or (ii) an occupational disease or infection that arises naturally and proximately out of employment covered under this chapter. The determination of eligibility for the benefit shall be made consistent with Title 51 RCW by the department of labor and industries. The department of labor and industries shall notify the department of retirement systems by order under RCW 51.52.050.

(b) The retirement allowance paid to the spouse and dependent children of a member who is killed in the course of employment, as set forth in RCW 41.05.011(14), shall include reimbursement for any payments of premium rates to the Washington state health care authority under RCW 41.05.080.

NEW SECTION. **Sec. 10.** This act is necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and takes effect immediately.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**11/06/2008**	**$150,000 Death Benefit**

WHAT THE READER SHOULD KNOW

The Office of the State Actuary ("we") prepared this draft fiscal note based on our understanding of the proposal as of the date shown above. We intend this draft fiscal note to be used by the Select Committee on Pension Policy throughout the 2008 Interim only. If a legislator introduces this proposal as a bill during the next Legislative Session, we will prepare a final fiscal note based on that bill language. The actuarial results shown in this draft fiscal note may change when we prepare our final version for the Legislature.

We advise readers of this draft fiscal note to seek professional guidance as to its content and interpretation, and not to rely upon this communication without such guidance. Please read the analysis shown in this draft fiscal note as a whole. Distribution of or reliance on only parts of this draft fiscal note could result in its misuse, and may mislead others.

SUMMARY OF RESULTS

This proposal increases the amount of the duty-related death benefit from $150,000 to $175,000. Current law provides the duty-related death benefit to members of all state retirement systems and other public employees who die from duty-related illnesses or injuries.

Impact on Pension Liability

(Dollars in Millions)	**Current**	**Increase**	**Total**
Today's Value of All Future Pensions	$67,081	$2.6	$67,083
Earned Pensions Not Covered by Today's Assets	$4,957	$0.1	$4,957

Impact on Contribution Rates: (Effective 9/1/2009)

2009-2011 State Budget	**PERS**	**TRS**	**SERS**	**PSERS**	**LEOFF**	**WSPRS**
Employee (Plan 2)	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Employer:						
Current Annual Cost	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Plan 1 Past Cost	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Total	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
State					0.00%	

Budget Impacts

(Dollars in Millions)	**2009-2011**	**2011-2013**	**25-Year**
General Fund-State	$0.0	$0.1	$3.5
Total Employer	$0.0	$0.4	$11.1

See the Actuarial Results section of this draft fiscal note for additional detail.

WHAT IS THE PROPOSED CHANGE?

Summary of Benefit Improvement

This proposal impacts the following retirement systems and public employees:

- Public Employees' Retirement System (PERS).
- Teachers' Retirement System (TRS).
- School Employees' Retirement System (SERS).
- Public Safety Employees' Retirement System (PSERS).
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF).
- Washington State Patrol Retirement System (WSPRS).
- Volunteer Firefighters' Relief and Pension Fund (VFF).
- Members of the Judicial Retirement System (JRS).
- Members of the Higher Education Retirement Plans (HIED).
- State, school district, and higher education employees who aren't members of a state retirement system.

This proposal increases the amount of the duty-related death benefit from $150,000 to $175,000.

Assumed Effective Date: Immediately upon passage

What Is The Current Situation?

The retirement systems and, in some cases, the state general fund pay a lump-sum death benefit for public employees who die as a result of a duty-related injury or illness. The amount of the benefit is currently $150,000. This benefit is provided for all members of PERS, TRS, SERS, PSERS, LEOFF, WSPRS, VFF, JRS, and HIED; and to state, school district and higher education employees who aren't members of a state retirement system. The lump-sum death benefit in VFF includes an additional $2,000.

Who Is Impacted And How?

This proposal could affect all 308,267 active members of the systems listed above through improved benefits. In addition, this proposal could affect 577 inactive fire fighters of LEOFF who are eligible for the benefit up to five years after separation of service. However, we only expect this benefit to be paid to about one member out of 24,500 members per year.

This proposal will increase the lump-sum death benefit by $25,000 for any member that dies as a result of a duty-related injury or illness.

Although this proposal does not produce supplemental contribution rate increases in the current biennium, this proposal impacts all 165,035 Plan 2 members of these systems through increased contribution rates in future biennia. With the exception of WSPRS members, this proposal will not affect member contribution rates in Plan 1 since they are fixed in statute. Additionally, this proposal will not affect member contribution rates in Plan 3 since Plan 3 members do not contribute to their employer-provided defined benefit.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

This proposal increases the amount of the lump-sum death benefit by $25,000. This increases the present value of future benefits of the affected systems. This proposal will not result in more lump-sum death benefits being paid, but when the benefits are paid, the amount will be larger.

Who Will Pay For These Costs?

Each system will subsidize the increase in liability that results from this proposal in their normal funding method:

- LEOFF 2: 50 percent member, 30 percent employer, and 20 percent State
- Plan 1: 100 percent employer
- Plan 2: 50 percent member and 50 percent employer
- Plan 3: 100 percent employer

HOW WE VALUED THESE COSTS

We changed the lump-sum duty death benefit to provide a $175,000 benefit in place of the current $150,000 benefit. We assumed no members of JRS will die from a duty-related illness or injury and have excluded these members from this pricing.

Otherwise, we developed these costs using the same assumptions, methods, assets, and data as disclosed in the June 30, 2007 Actuarial Valuation Report (AVR).

We used the Entry Age Normal actuarial funding method to determine the fiscal budget changes for future new entrants. We used the Aggregate actuarial funding method to determine the fiscal budget changes for current plan members.

ACTUARIAL RESULTS

How The Liabilities Changed

This proposal will impact the actuarial funding of the plans by increasing the present value of future benefits payable under the plans as shown in the following table.

Impact on Pension Liability

(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits			
(The Value of the Total Commitment to all Current Members)			
PERS 1	$14,061	$0.0	$14,061
PERS 2/3	20,634	0.7	20,635
PERS Total	**34,695**	**0.7**	**34,696**
TRS 1	11,021	0.0	11,021
TRS 2/3	7,078	0.1	7,078
TRS Total	**18,099**	**0.1**	**18,099**
SERS 2/3	**2,698**	**0.2**	**2,698**
PSERS 2	**225**	**0.0**	**225**
LEOFF 1	4,358	0.1	4,358
LEOFF 2	6,149	1.5	6,151
LEOFF Total	**10,507**	**1.6**	**10,509**
WSPRS 1/2	**$856**	**$0.0**	**$856**
Unfunded Actuarial Accrued Liability			
(The Portion of the Plan 1 Liability that is Amortized to 2024)			
PERS 1	**$3,609**	**$0.0**	**$3,609**
TRS 1	**2,288**	**0.0**	**2,288**
LEOFF 1	**($939)**	**$0.1**	**($939)**
Unfunded PUC Liability			
(The Value of the Total Commitment to all Current Members Attributable to Past Service that is not covered by current assets)			
PERS 1	$3,990	$0.0	$3,990
PERS 2/3	(2,470)	0.7	(2,469)
PERS Total	**1,520**	**0.7**	**1,521**
TRS 1	2,552	0.0	2,552
TRS 2/3	(1,229)	0.1	(1,229)
TRS Total	**1,323**	**0.1**	**1,323**
SERS 2/3	**(443)**	**0.2**	**(443)**
PSERS 2	**(2)**	**0.0**	**(2)**
LEOFF 1	(975)	0.1	(975)
LEOFF 2	(974)	1.5	(972)
LEOFF Total	**(1,949)**	**1.6**	**(1,947)**
WSPRS 1/2	**($121)**	**$0.0**	**($121)**

Note: Totals may not agree due to rounding.

In addition, this proposal increases the pension liability of the VFF pension plan by $128,000.

We did not value the impact of this proposal on the following members since we do not currently value them in any of our actuarial valuations:

- 2,854 Volunteer Fire Fighters that are not members of the pension plan;
- Members of HIED; and
- State, school district, and higher education employees who aren't members of the Washington State Retirement Systems.

How Contribution Rates Changed

The increase in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01%, therefore the proposal will not affect contribution rates in the current biennium. However, we will use the un-rounded rate increase to measure the fiscal budget changes in future biennia.

Impact on Contribution Rates: (Effective 9/1/2009)

System/Plan	PERS	TRS	SERS	PSERS	LEOFF	WSPRS
Current Members						
Employee (Plan 2)	0.001%	0.000%	0.001%	0.000%	0.005%	0.003%
Employer:						
Normal Cost	0.001%	0.000%	0.001%	0.000%	0.003%	0.003%
Plan 1 UAAL	0.000%	0.000%	0.000%	0.000%	0.000%	0.000%
Total	0.001%	0.000%	0.002%	0.000%	0.003%	0.003%
State					0.002%	
New Entrants*						
Employee (Plan 2)	0.001%	0.000%	0.002%	0.001%	0.008%	0.005%
Employer:						
Normal Cost	0.001%	0.000%	0.002%	0.001%	0.005%	0.005%
Plan 1 UAAL	0.000%	0.000%	0.000%	0.000%	0.000%	0.000%
Total	0.001%	0.000%	0.002%	0.001%	0.005%	0.005%
State					0.003%	

**Rate change applied to future new entrant payroll and used to determine budget impacts only. Current members and new entrants pay the same contribution rate.*

How This Impacts Budgets And Employees

Budget Impacts							
(Dollars in Millions)	**PERS**	**TRS**	**SERS**	**PSERS**	**LEOFF**	**WSPRS**	**Total**
2009-2011							
General Fund	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Non-General Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total State	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Local Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Employer	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2011-2013							
General Fund	$0.0	$0.0	$0.0	$0.0	$0.1	$0.0	$0.1
Non-General Fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total State	**0.1**	**0.0**	**0.0**	**0.0**	**0.1**	**0.0**	**0.2**
Local Government	0.1	0.0	0.0	0.0	0.1	0.0	0.2
Total Employer	**0.1**	**0.0**	**0.1**	**0.0**	**0.2**	**0.0**	**0.4**
Total Employee	**$0.1**	**$0.0**	**$0.0**	**$0.0**	**$0.2**	**$0.0**	**$0.3**
2009-2034							
General Fund	$0.6	$0.2	$0.6	$0.0	$2.1	$0.0	$3.5
Non-General Fund	0.9	0.0	0.0	0.0	0.0	0.2	1.1
Total State	**1.5**	**0.2**	**0.6**	**0.0**	**2.1**	**0.2**	**4.6**
Local Government	2.3	0.1	0.9	0.0	3.1	0.0	6.5
Total Employer	**3.9**	**0.4**	**1.5**	**0.0**	**5.1**	**0.2**	**11.1**
Total Employee	**$2.6**	**$0.2**	**$0.9**	**$0.0**	**$5.1**	**$0.2**	**$9.1**

Note: Totals may not agree due to rounding.

The analysis of this proposal does not consider any other proposed changes to the systems. The combined effect of several changes to the systems could exceed the sum of each proposed change considered individually.

As with the costs developed in the actuarial valuation, the emerging costs of the systems will vary from those presented in the AVR or this draft fiscal note to the extent that actual experience differs from the actuarial assumptions.

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

To determine the sensitivity of the actuarial results to the best-estimate assumptions used in this pricing, we varied the duty-related death assumption for LEOFF 2. We chose LEOFF 2 for our sensitivity testing for two reasons:

1. We developed our current duty-related death assumptions for LEOFF 2 in 2006 and 2007 in response to new laws for duty-related injuries and illnesses. We have not had sufficient experience in the plan to determine if these assumptions are accurate in the long-term. As a result, there is a higher risk for this pricing with LEOFF 2.

2. If we experience any catastrophic events impacting duty-related injuries or illnesses that result in death, we expect this will affect our law enforcement officers and fire fighters. A single catastrophic event, while short-term, could add a significant cost to the plan, particularly with lump-sum benefits.

We changed the duty-related death assumption by doubling the rate of deaths that we expect will result from a duty-related injury or illness. We did not increase our mortality assumptions, only the number of deaths that are duty-related. The next table shows our current assumptions ("Base Assumptions") and increased assumptions ("Sensitivity Assumptions").

	Base Assumptions	**Sensitivity Assumptions**
Duty Death Rate	0.0376%	0.0752%
Occupational Disease Death Rate (Fire Fighters only)		
Age 20-49	14.742%	29.484%
Age 50+	27.393%	54.786%

The result of increasing the rate of deaths from a duty-related injury or illness is detailed in the following table. We compare the assumptions used in this proposal ("Best Estimate Pricing") with the increased assumptions ("Sensitivity Pricing") to show the sensitivity of this pricing proposal on the duty-related death assumptions.

(Dollars in Millions)	**Best Estimate Pricing**	**Sensitivity Pricing**
Liability Increase	$1.5	$2.4
Contribution Rate Increase		
Employee	0.005%	0.008%
Employer	0.003%	0.005%
State	0.002%	0.003%
Budget Impacts		
2009-2011		
General Fund - State	$0.0	$0.0
Total Employer	$0.0	$0.3

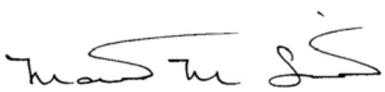
There is also a possibility that fewer duty-related deaths will occur than we assume for LEOFF 2 in the future. If we tested lower rates, we would expect lower costs than our pricing of this proposal shows.

ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost and asset valuation methods are appropriate for the purposes of this pricing exercise.
2. The actuarial assumptions used are appropriate for the purposes of this pricing exercise.
3. The data on which this draft fiscal note is based are sufficient and reliable for the purposes of this pricing exercise.
4. Use of another set of methods and assumptions may also be reasonable, and might produce different results.
5. This draft fiscal note has been prepared for the Select Committee on Pension Policy.
6. This draft fiscal note has been prepared, and opinions given, in accordance with Washington State law and accepted actuarial standards of practice as of the date shown on page 1 of this draft fiscal note.

This draft fiscal note is a preliminary actuarial communication and the results shown may change. While this draft fiscal note is meant to be complete, the undersigned is available to provide extra advice and explanations as needed.



Matthew M. Smith, FCA, EA, MAAA
State Actuary

GLOSSARY OF ACTUARIAL TERMS

Actuarial Accrued Liability: Computed differently under different funding methods, the actuarial accrued liability generally represents the portion of the present value of fully projected benefits attributable to service credit that has been earned (or accrued) as of the valuation date.

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of actuarial assumptions (i.e. interest rate, rate of salary increases, mortality, etc.).

Aggregate Funding Method: The Aggregate Funding Method is a standard actuarial funding method. The annual cost of benefits under the Aggregate Method is equal to the normal cost. The method does not produce an unfunded liability. The normal cost is determined for the entire group rather than on an individual basis.

Entry Age Normal Cost Method (EANC): The EANC method is a standard actuarial funding method. The annual cost of benefits under EANC is comprised of two components:

- Normal cost.
- Amortization of the unfunded liability.

The normal cost is determined on an individual basis, from a member's age at plan entry, and is designed to be a level percentage of pay throughout a member's career.

Normal Cost: Computed differently under different funding methods, the normal cost generally represents the portion of the cost of projected benefits allocated to the current plan year.

Projected Unit Credit (PUC) Liability: The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date (past service).

Projected Benefits: Pension benefit amounts which are expected to be paid in the future taking into account such items as the effect of advancement in age as well as past and anticipated future compensation and service credits.

Unfunded PUC Liability: The excess, if any, of the Present Value of Benefits calculated under the PUC cost method over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.

Unfunded Actuarial Accrued Liability (UAAL): The excess, if any, of the actuarial accrued liability over the actuarial value of assets. In other words, the present value of benefits earned to date that are not covered by plan assets.

The Select Committee on Pension Policy

$150,000 Death Benefit

Darren Painter, Policy Analyst

November 18, 2008

Office of the State Actuary

"Securing tomorrow's pensions today."

What Is The Issue?

- Amount of death benefit hasn't changed since 1996
- LEOFF 2 Board asked SCPP to revisit inflation adjustment
- Key policy questions
  - Is the current amount sufficient or should it be adjusted for past inflation?
  - Should the benefit be protected against future inflation?

Committee Activity

- Briefing in October
  - Included options
- Chair requested pricing on new option
- Opportunity for formal action today

What Is The Benefit?

- $150,000 lump sum for duty-related death (injury or illness)
  - Provided in all retirement systems
  - Designed to provide temporary financial assistance
- Amount hasn’t changed since benefit established
- Actuaries expect fewer than 13 duty-deaths a year

Options Studied In October

- Option 1: Adjust for past inflation
  - Increase to $205,000
- Option 2: Automatically adjust for future inflation
  - COLA on current amount
- Option 3: Adjust for past and future inflation
  - Increase to $205,000 + COLA

New Option Requested By Chair

- Option 4: Increase benefit to $175,000
- Partial adjustment
  - Recovers some, not all, value lost to inflation
- Doesn't protect against future inflation
- Bill draft and draft fiscal note in materials

Two Key Policy Decisions

- How much value to recover?
  - None to all
- How much control to retain?
  - Some or full
  - Automatic COLAs require policy makers to give up some control

Preliminary Total Employer Rate Increase

System	Option 1 Adjust past inflation ($205,000)	Option 2 Automatic CPI-based COLA	Option 3 Adjust past inflation + Automatic COLA	Option 4 Partial adjustment ($175,000)
PERS	*	*	*	*
TRS	*	*	*	*
SERS	*	*	.01%	*
PSERS	*	*	*	*
LEOFF	.01%	.01%	.01%	*
WSPRS	.01%	*	.01%	*

**Insufficient to immediately impact rates.*

Preliminary Fiscal Costs

($ in millions)	Option 1 Adjust past inflation ($205,000)	Option 2 Automatic CPI-based COLA	Option 3 Adjust past inflation + Automatic COLA	Option 4 Partial adjustment ($175,000)
2009-2011				
Total GFS	$0.0	$0.0	$0.4	$0.0
Total Employer	0.3	0.3	0.9	0.0
25 Year				
Total GFS	6.8	2.4	10.4	3.5
Total Employer	$22.5	$7.6	$33.0	$11.1

Possible Next Steps

- Recommend to Legislature the bill increasing the death benefit to $175,000
- Develop a proposal based on other options
  - Staff will prepare draft legislation
  - Public hearing in December
- Study other options
- Consider this briefing informational and take no further action