PERS To SERS Auto-Transfer

Description Of Issue

There are statutory provisions to automatically transfer the membership and service credit of certain Public Employees' Retirement System (PERS) Plan 2 members into the School Employees' Retirement System (SERS). This "auto-transfer" was designed to move classified school employees to SERS when the system first opened in 2000.

Policy Highlights

- The advantages of the auto-transfer have diminished since the initial creation of SERS.
- The auto-transfer may be impacting members never intended—most notably PERS 2 members whose primary careers are unrelated to school employment.
- Continuing the auto-transfer may lead to potential legal risk in the future.

Policy Options

- **Target Auto-transfer To Former School Employees.**
  - More consistent with Legislative intent.
  - Eliminates most member complaints.
  - Doesn't address concerns about potential legal risk of continuing the transfer indefinitely.
- **End Auto-transfer.**
  - There is less need for the auto-transfer today.
  - Potential legal risk increases the longer the transfer continues.
  - Members may receive full value for prior school employment in PERS under dual-membership provisions.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 session to end the auto-transfer and allow certain affected members to reverse it (HB 3005/SB 6655). The 2008 SCPP bill did not pass the Legislature, but did pass the House and the Senate Committee on Ways & Means.

The Committee held a public hearing and took executive action on this issue in May of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 session.

Recommendation To 2009 Legislature

End the conditional automatic transfer of membership from PERS to SERS and allow certain auto-transferred members to reverse the transfer.

Staff Contact

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PERS to SERS Auto-Transfer

In Brief

ISSUE

The membership and service credit of certain PERS 2 members is being automatically transferred to SERS. This transfer, which was designed to move classified school employees to SERS when the system was first opened, occurs even if the member's primary career is unrelated to school employment.

The statutes governing the transfer of PERS membership to SERS may be impacting members that the Legislature did not intend to impact. Further, the open-ended nature of the auto-transfer may lead to unintended consequences in future years.

MEMBER IMPACT

On average, nearly 50 PERS 2 members a month have their membership and service credit transferred to SERS.*

**As of June, 2007.*

Dave Nelsen
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Current Situation

There are statutory provisions to automatically transfer the membership and service credit of certain Public Employees' Retirement System (PERS) Plan 2 members to the School Employees' Retirement System (SERS) Plan 2. This will be referred to as the "auto-transfer" throughout this paper. Affected members have their PERS membership and service credit automatically transferred to SERS if they become employed in a SERS eligible position*. If the member has withdrawn any contributions, such contributions and the associated service credit may be restored to SERS. PERS 2 members currently being affected by the auto-transfer provisions if they become employed in a SERS eligible position* include:

- Members who first entered PERS employment after SERS was opened.
- Members who were working for non-educational employers when SERS was opened.
- Members who left or retired from PERS employment prior to the opening of SERS.
- Members whose last employment was for a school district or educational district and who retired from PERS 2 prior to the opening of SERS and opt to re-establish membership.

A PERS 2 member's service and membership will only be automatically transferred to SERS one time – even if the member alternates between PERS and SERS positions throughout their career in public service.

**Or establish membership in SERS as a substitute employee.*

History

The SERS system was created in 1998 and opened to membership on September 1, 2000. Initial membership was comprised of PERS 2 members who were employed by school districts and educational service districts on September 1, 2000.

The intent of the Legislature in creating SERS was "to achieve similar retirement benefits for all educational employees by transferring the membership of classified school employees in [PERS 2] to [SERS 2]. The transfer of membership to [SERS 2] is not intended to cause a diminution or expansion of benefits for affected members. It is enacted solely to provide public employees working under the same conditions with the same options for retirement planning." See RCW 41.35.005.

SERS was created to allow classified school employees access to Plan 3 benefits.

When the SERS system was created, Plan 3 had been established for teachers, but not for public employees. At that time, classified school employees in PERS wanted the same Plan 3 benefits that were available to teachers. SERS was created to provide that option. SERS featured both a Plan 2 and a Plan 3 when it was created. SERS Plan 2 had the same benefit structure as PERS Plan 2, and SERS Plan 3 had the same benefit structure as the Teachers' Retirement System (TRS) Plan 3. PERS 2 members employed in SERS-eligible positions on the day SERS opened were initially transferred to SERS 2 - where they then had the opportunity to transfer to SERS 3. The transfer of all service, and corresponding contributions, from PERS 2 to SERS 2 provided members who were intending to transfer to SERS 3 the largest possible balance in their SERS Plan 3 defined contribution accounts.

The transfer of PERS 2 members to SERS 2 was extended beyond the initial opening date of SERS.

The transfer of PERS 2 members to SERS 2 was extended beyond the initial opening date of SERS. PERS 2 members who were not employed in a SERS-eligible position when SERS first opened have their PERS 2 membership and service transferred to SERS 2 if they later become employed in a SERS-eligible position. This transfer is accomplished through means of the auto-transfer statutes (see **Current Situation** above for a complete description). In addition to returning school employees, the auto-transfer is impacting PERS members whose primary careers are unrelated to school employment.

Since the initial transfer of PERS 2 classified school employees to SERS 2, over 5,000* PERS 2 members who became employed in SERS eligible positions have had their PERS membership and service credit automatically transferred to SERS. It is unknown how many of these members' PERS service was related to school employment. The Department of Retirement Systems has received complaints from some members who have had their PERS 2 service automatically transferred to SERS 2 when their primary career was not in SERS.

During the 2004 Legislative Session a bill was introduced that would have removed the provisions for the automatic transfer of PERS 2 members into SERS 2 upon employment in a SERS eligible position. This bill (SB 6610) did not go through the SCPP and did not receive a hearing.

**As of June, 2007.*

Examples

Example 1: School Employee With Break In Service

A PERS 2 member employed by a school district leaves employment after five years of service and prior to the opening of SERS. Two years later the member returns to an eligible position in a school district. The member's five years of prior PERS 2 service are automatically transferred to SERS 2.

Example 2: County Employee Taking A Part-Time SERS job

PERS members taking a part-time SERS job for the first time have their PERS membership automatically transferred to SERS.

A county employee with 15 years of service in PERS 2 takes an additional part-time job with a school district to earn extra money. This is the first time the member has held a SERS-eligible position. Because the member is now employed in a SERS-eligible position, his PERS membership and 15 years of PERS service are automatically transferred to SERS. Any future service rendered for the county remains in PERS.

Policy Analysis

Possible Inconsistency With SERS Intent

The PERS to SERS auto-transfer allows classified school employees who experienced a break in service when SERS first opened to transfer their past service into SERS if they become re-employed in a SERS-eligible position. This is in keeping with the Legislature's stated intent to "provide public employees working under the same conditions with the same options for retirement planning". See RCW 41.35.005. However, the auto-transfer also transfers the membership and service credit of PERS members whose primary careers are unrelated to school employment. This appears to be inconsistent with the original intent of the Legislature in creating SERS. It is possible that the auto-transfer was designed around career school employees. Little consideration may have been given to PERS members who take part-time SERS positions in addition to their primary PERS career. The Legislature may not have intended the auto-transfer statutes to impact PERS members whose primary careers are unrelated to school employment.

The Legislature may not have intended the auto-transfer statutes to impact PERS members whose primary careers are unrelated to school employment.

Clarifying the language in the existing statutes so the auto-transfer only impacts former school employees would be more consistent with the Legislature's original intent. Such a fix would likely eliminate most, if not all, of the member complaints about the auto-transfer process. However, even if the auto-transfer statutes were amended to only impact this group, there are still policy concerns with having an open-ended auto-transfer.

Implications Of Continuing The Auto-Transfer

Continuing the PERS to SERS auto-transfer may not make as much sense today.

While it may have made sense when SERS was first opened to transfer members' service over from PERS, it may not make as much sense to continue that policy today. Transferring prior PERS service into SERS would have simplified the initial transfer process from both the member's and plan administrator's perspective. From the member's perspective, having all of one's service in a single plan makes retirement planning less complicated. Transferring the prior PERS service provided SERS members the same opportunity that teachers had to move their Plan 2 service into Plan 3 and maximize their Plan 3 defined contribution accounts. This was consistent with the legislative intent to achieve similar retirement benefits for all educational employees. See RCW 41.35.005. From the administrator's perspective, a one-time transfer may have been preferable to maintaining over 40,000 new dual-members.

The advantages of the auto-transfer have diminished since the initial creation of SERS.

The advantages of the auto-transfer, however, have diminished since the initial creation of SERS. The number of former classified school employees returning to service and being impacted by the auto-transfer is relatively small compared to the initial number who transferred to SERS. Some of these members have already experienced a fairly long break in service - nearly seven years – or transitioned to public employment outside of a school district. This raises the question of whether special accommodations should be made for these members if they return to classified school employment. Since PERS now has a Plan 3 and experience has shown that members are generally less interested in transferring from Plan 2 to Plan 3 today, there is likely less need to provide a mechanism for members to transfer prior PERS 2 service into SERS 3. Additionally, it is not guaranteed that benefits will be the same in PERS 2 and SERS 2 in the future, which may result in unintended consequences.

When SERS was first created, the benefit provisions of SERS 2 and PERS 2 were identical. Thus, members did not experience either a diminution or expansion of benefits by having their PERS 2 membership and service transferred to SERS 2. However, the more time that passes following the creation of SERS, the greater the likelihood that the benefit provisions of PERS 2 and SERS 2 will start to diverge. Divergent benefits often result from pension legislation that does not go through a policy committee like the SCPP. If the differences in the plans were to become substantial enough, members may actually begin to experience a diminution or expansion of benefits by having their PERS membership automatically transferred to SERS. Such an outcome was likely not envisioned as a possibility at that time and was clearly not part of the Legislature's original intent in transferring members to SERS (see RCW 41.35.005). If benefits were to diverge to the point that some members were being inadvertently harmed by the auto-transfer, it may create potential legal risk for the state.

In the future, there could be increased legal risk.

Given the diminished benefits of the auto-transfer today and the potential legal risk that may arise from a mandatory transfer of membership in the future, it may be preferable from both a policy and administrative perspective to discontinue the auto-transfer. Policy makers may wish to consider making the transfer of prior PERS 2 service to SERS optional for returning educational employees, or as an alternative, allowing such employees to become dual-members.

Implications For Dual-Membership

Transferring service credit between systems is counter to the policy of dual-membership which is codified within the "portability" chapter of state law (see RCW 41.54). Dual-membership allows members to combine service from all their systems to qualify for benefits and use the highest salary from any system to determine their benefits. Each system then pays out benefits based on that system's provisions and the service in that system. Dual-membership is designed to ensure that members are neither advantaged nor disadvantaged by changing public careers – even when the underlying benefits of the systems differ.

Members may still receive full value for past school employment under dual-membership provisions.

While dual-membership will effectively make "whole" the retirement benefits for classified school employees whose service crosses from PERS to SERS, it is not an exact substitute for transferring service. Members may still receive full value for their past school employment in PERS under the dual-membership provisions; however, they would not be able to transfer their prior Plan 2 service into Plan 3 as they would under the auto-transfer provisions*. Currently, very few active members opt to transfer from Plan 2 to Plan 3 under the annual transfer window. Cases where a returning classified school employee would wish to transfer all their past Plan 2 service to Plan 3 will likely be the exception.

The PERS to SERS auto-transfer is an exception to the basic policy of dual-membership. Maintaining such an exception may, in rare cases, benefit a few members. However, policy makers may wish to weigh the potential benefits against the potential legal risk.

**The member's PERS 2 service would be transferred to SERS 2 and the member could later opt to transfer that service to SERS 3.*

Implications for Optional Transfer

Making the auto-transfer optional instead of mandatory would reduce the risk of the exposure to one kind of liability while increasing the risk of exposure to another. Making

An optional transfer may result in a cost to other plan members or employers.

the transfer optional would likely eliminate the potential legal risk of members being harmed by the transfer. However, members may be able to take advantage of an optional transfer to increase their benefits while passing the cost of those benefits on to others. This situation could occur if the benefits in SERS were to become more generous than the benefits in PERS. Members electing to transfer their service would essentially be able to "buy" the more expensive SERS benefits using cheaper PERS service. This would result in a cost to the SERS system which would be subsidized by all plan members and/or employers.

Other States

Due to the narrow focus and technical nature of this issue, the experience of other states, if any, would be of limited value to policy makers and would be impractical to obtain.

Policy Questions

Policy makers may wish to consider the following questions when deliberating on this issue:

- Should the auto-transfer statutes be amended so that they only impact members whose prior PERS service was rendered for a school or educational service district?
- Should the PERS to SERS auto-transfer be made optional? Discontinued? If discontinued, what is the appropriate date to discontinue it?

Conclusion

The PERS to SERS auto-transfer was designed to facilitate the initial creation of the SERS system for classified school employees. The auto-transfer was extended beyond the initial opening date of SERS, and is impacting both returning school employees and PERS members whose primary careers are unrelated to school employment. The Legislature may not have intended to impact this latter group of PERS members.

The automatic transfer of PERS 2 membership and service to SERS 2 at the initial opening of SERS was advantageous for both members and the plan administrator. The advantages of the auto-transfer; however, have diminished since the initial creation of SERS. Continuing the mandatory auto-transfer indefinitely may expose the state to potential legal risk if the benefits in SERS 2 and PERS 2 diverge in the future. Making the auto-transfer optional would eliminate one source of potential liability, but it may result in costs being shifted to other SERS members or employers. In the absence of transfer provisions, SERS members may still receive full value for any past school employment in the PERS system under dual-membership provisions.

Policy makers may wish to weigh the potential benefits and risks of continuing the auto-transfer.

Policy makers may wish to weigh the potential benefits against the potential risks of continuing the auto-transfer in its present form.

Committee Activity

The SCPP studied this issue in 2007 and recommended a bill in the 2008 Session to end the auto-transfer and allow certain affected members to reverse it (HB 3005/SB 6655). The 2008 SCPP bill did not pass the Legislature, but did pass the House and the Senate Committee on Ways & Means.

The Committee held a public hearing and took executive action on this issue in May of 2008. The Committee moved to reintroduce the 2008 SCPP bill for the 2009 Session.

Executive Committee Recommendation

None.

Recommendation To 2009 Legislature

End the conditional automatic transfer of membership from PERS to SERS and allow certain auto-transferred members to reverse the transfer. Recommended May 13, 2008.

Stakeholder Input

Correspondence on file from:

John Kvamme, WASA & AWSP consultant, 4/15/2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0071.2/09).

Draft Fiscal Note

Attached.

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BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0071.2/09 2nd draft

ATTY/TYPIST: LL:seg

BRIEF DESCRIPTION: Transferring public employees' retirement system plan 2 members to the school employees' retirement system plan 2.

AN ACT Relating to the transfer of public employees' retirement system plan 2 members to the school employees' retirement system plan 2; and amending RCW 41.40.750.

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

Sec. 1. RCW 41.40.750 and 2001 2nd sp.s. c 10 s 13 are each amended to read as follows:

(1) Effective September 1, 2000, the membership of all plan 2 members currently employed in eligible positions in a school district or educational service district and all plan 2 service credit for such members, is transferred to the Washington school employees' retirement system plan 2. Plan 2 members who have withdrawn their member contributions for prior plan 2 service may restore contributions and service credit to the Washington school employees' retirement system plan 2 as provided under RCW 41.40.740.

(2)(a) The membership and previous service credit of a plan 2 member not employed in an eligible position on September 1, 2000, will be transferred to the Washington school employees' retirement system plan 2 when he or she becomes employed in an eligible position <u>prior to August 1, 2009</u>. Plan 2 members not employed in an eligible position on

September 1, 2000, who have withdrawn their member contributions for prior plan 2 service may restore contributions and service credit to the Washington school employees' retirement system plan 2 as provided under RCW 41.40.740, if they first establish eligibility in the Washington school employees' retirement system plan 2 prior to August 1, 2009.

(b) The membership and previous service credit of a plan 2 member last employed by a school district or educational service district and retired prior to September 1, 2000, will be transferred to the Washington school employees' retirement system plan 2 if the member opts to reestablish membership prior to August 1, 2009.

(3) Members who restore contributions and service credit under subsection (1) or (2) of this section shall have their contributions and service credit transferred to the Washington school employees' retirement system.

(4) From September 1, 2009, through November 30, 2009, upon written request to the department, active and inactive members transferred under subsection (2) of this section who did not establish membership and earn service credit for employment with a school district or educational service district prior to the transfer, and who have not transferred to plan 3 of the Washington school employees' retirement system or plan 3 of the public employees' retirement system, may restore their transferred membership and previous service credit to plan 2. All previously transferred contributions and interest, and additional interest as determined by the department, shall be returned to plan 2. An additional amount shall be transferred from the Washington school employees' retirement system sufficient to offset the liabilities returned to plan 2 under this subsection, as determined by the state actuary.

--- END ---

DRAFT
ACTUARY'S FISCAL NOTE

RESPONDING AGENCY:	CODE:	DATE:	PROPOSAL [NAME or Z-NUMBER]:
Office of the State Actuary	**035**	**12/19/08**	**Z-0071.2 / Z-0392.1**

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 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

No change to the unfunded liabilities of the affected systems.

This proposal gives certain School Employees' Retirement System (SERS) members who had service automatically transferred from the Public Employees' Retirement System (PERS) the option to move their service and associated savings funds back to PERS. This proposal provides for an additional transfer of assets from SERS to PERS to offset the liability transferred to PERS.

Passage of this proposal would result in a transfer of liabilities of about $28.1 million to PERS from SERS. Transfers of savings funds and additional assets from SERS to PERS totaling $11.5 million and $16.6 million, respectively, totally offset the transferred liability. Because the transfer of assets fully offsets the transfer of liabilities, this proposal will not affect the contribution rates of either PERS or SERS.

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

WHAT IS THE PROPOSED CHANGE?

Summary of Change

This proposal impacts PERS Plan 2 and SERS Plan 2 by amending RCW 41.40.750 to do the following:

- Stop the automatic transfer of prior PERS Plan 2 service to SERS Plan 2:
    - Upon employment in a SERS eligible position. Prior PERS Plan 2 members hired into SERS eligible positions after the proposal's effective date become dual members under the provisions of Chapter 41.54 RCW.
    - For former PERS Plan 2 members who worked in SERS eligible positions, retired prior to September 1, 2000, later returned to work in a SERS eligible position, and opted back into SERS membership.
- Remove the requirement to restore withdrawn prior PERS Plan 2 service in SERS Plan 2. Restorations for members hired after the proposal's effective date will occur under the dual membership provisions of Chapter 41.54 RCW.
- Provide a three month window for current and former SERS Plan 2 members to choose to reverse the transfer of prior PERS Plan 2 service and savings accounts. To reverse the transfer members must have:
    - Not worked in a SERS eligible position prior to their transfer.
    - Been automatically transferred after September1, 2000.
- Transfer additional funds from the SERS Plan 2 trust fund to the PERS Plan 2 trust fund to offset the liability transferred to PERS under this proposal.

Assumed Effective Date: 90 days after session.

What Is The Current Situation?

The provisions of RCW 41.40.750 provide the following:

- All prior PERS Plan 2 members hired into SERS eligible positions after September 1, 2000, have their PERS Plan 2 membership automatically transferred to SERS Plan 2.
- SERS Plan 2 members who withdrew prior PERS Plan 2 service must restore that service in SERS Plan 2.
- PERS Plan 2 members who worked in a SERS eligible position, retired prior to September 1, 2000, and opt into membership upon employment in a SERS eligible position will have their prior service in PERS Plan 2 transferred to SERS Plan 2.

Who Is Impacted And How?

We estimate that 5,799 PERS members had service transferred to SERS after September 1, 2000. Of those we estimate this proposal impacts about 1,860 members by giving them the ability to move their service and associated savings funds back to PERS. The affected members include actives, terminated vested members, and Terminated Non-Vested (TNV) members. TNV members can only receive their contributions with interest.

This proposal also impacts members who withdrew their PERS service and savings funds, but upon becoming a SERS member had the right to restore that service credit. We estimate that 1,915 members had a right to restore PERS service credit automatically transferred to SERS. Since these members withdrew their PERS service, no service credit was transferred to SERS. These members have five years from the time they become SERS members to restore their PERS service for a subsidized amount. After five years the members can still restore the withdrawn service credit, but they must pay the full actuarial value.

We don't believe the members impacted by this proposal will receive improved benefits. The only difference between the benefits in PERS 2 and SERS 2 is the availability of a 200 percent refund of contributions benefit for PERS 2 members who interrupt their PERS service to join the uniformed services and are subsequently killed while on active duty.

See the Special Data Needed section of this draft fiscal note for more details.

WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has A Cost

Transferring service from SERS to PERS decreases the pension costs in SERS and increases them in PERS. To offset the pension cost change this proposal transfers the savings funds back to PERS from SERS attributable to the transferred service. The transfer of savings funds in most cases does not fully offset the transferred pension costs for two main reasons. First, this proposal transfers only the member contributions not the employer contributions. Second, the Department of Retirement Systems (DRS) credits 5.5 percent interest to the savings funds. But we assume 8 percent interest when we calculate the liabilities. This difference in credited and assumed interest implies the assets will never accumulate in the members' saving funds at a high enough rate to cover the cost of their pensions.

In a few cases the accumulated value of a member's savings fund exceeds the value of the transferred service. We believe this situation results for a few reasons: decreases in a member's salary, changes in a member's working status, or both.

When a member's salary decreases, so does their Average Final Compensation (AFC). A lower AFC leads to lower liabilities. Also the contributions collected on the prior higher salaries lead to higher savings funds relative to the liabilities calculated on current lower salaries. Since the data we have only shows current salaries, we cannot identify specific cases where lower salaries lead to savings funds being more valuable than the associated liabilities.

Members who no longer work in a pension system do not receive salary increases. Since these members' salaries don't increase, neither does their AFC. This leads to lower liabilities. Also the contribution rates charged while the member worked reflected the assumption that members would continue to receive salary increases. The result is again that the savings funds for these members transferred back to PERS exceed the corresponding liabilities.

For members who withdrew their PERS service prior to taking a position with a SERS employer, DRS transferred the members' right to restore service credit to SERS. This proposal provides that members who restore PERS service credit in SERS can elect to move the restored service and associated savings fund back to PERS.

Who Will Pay For These Costs?

The proposal mandates an additional asset transfer from the SERS trust fund to the PERS trust fund to fully offset the change in pension cost. As a result this proposal does not impact contribution rates in either PERS or SERS.

HOW WE VALUED THESE COSTS

Assumptions We Made

For each member we determined the value of their eligible prior PERS service and the value of the savings funds attributable to that service as of June 30, 2007. The value of the service depends on when we expect the member to retire and how much salary they earned prior to retirement. The value of the savings fund only depends on when the member transferred.

We assumed all members would retire at the earliest of the following:
- Upon reaching 30 years of service between ages 55 and 65.
- At age 65.
- Immediately if currently older than age 65.

Finally, the amount of the total liability and assets transferred back to PERS depends on the number of people who elect to participate under this proposal. The liabilities and assets shown in this draft fiscal reflect that we valued this proposal assuming every member who could transfer would.

For more detail please see Appendix A.

How We Applied These Assumptions

We used a spreadsheet model to apply the assumptions to the individual members impacted by this proposal. We used the SERS salary growth and mortality assumptions to determine the value of the liability for each member. We accumulated each member's savings fund with interest to the valuation date. The assets required to ensure this proposal doesn't impact contribution rates equals the difference between the liabilities and savings funds.

For more detail please see Appendix B.

Special Data Needed

DRS provided a data file containing records for the 5,799 members automatically transferred from PERS to SERS since September 1, 2000. This data file contained the months of service, the savings fund balance transferred for each member, the date the service and savings funds transferred, the plans in both PERS and SERS the members were in, and whether or not the member had prior service in PERS for an educational employer. We relied upon this data as complete and accurate. We combined this data file with the PERS and SERS 2007 valuation data to determine each member's current status, current salary, and total service.

The data DRS provided doesn't identify members who restored PERS service in SERS. As of the date of this draft fiscal note we requested an updated data file from DRS. We will include the results in the final fiscal note we produce for the 2009 Legislative Session. We did not attempt to value liability for members who could restore prior PERS service credit in SERS and elect to transfer that service credit back to PERS under this proposal.

For more details please see Appendix C.

ACTUARIAL RESULTS

How The Liabilities Changed

The transfer of service from SERS Plan 2 to PERS Plan 2 will result in a liability decrease in SERS and a liability increase in PERS. This liability represents the value in today's dollars of all the future pension payments we expect DRS to pay as a result of the service transferred. This proposal also transfers from SERS Plan 2 to PERS Plan 2 the accumulated value of the member contributions paid at time the member earned the service. This asset transfer will result in a decrease in SERS assets and an increase in PERS assets. Since the accumulated value of all the savings funds does not exceed the value of the future pension payments, this proposal mandates that SERS transfer additional assets to PERS to ensure the contribution rates stay the same in both systems.

The following table summarizes the results.

Table 1

Summary of Liabilities and Assets Expected to be Transferred

	System/Plan	
(Dollars in Millions)	**PERS 2**	**SERS 2**
Liability change	$28.1	-$28.1
Savings Fund asset change	11.5	-11.5
Additional asset transfer	16.6	-16.6
Change in Unfunded Liability	$0.0	$0.0

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

As with the costs developed in the actuarial valuation, the emerging costs of the system will vary from those presented in the 2007 Actuarial Valuation Report (AVR) or this fiscal note to the extent that actual experience differs from the actuarial assumptions.

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

We did not perform specific sensitivity tests for this pricing. The liabilities and assets calculated for this fiscal note depend heavily on the number of members transferring service from SERS back to PERS. If half of the 1860 members elect to transfer service back to PERS, we would expect the liabilities and assets to be approximately half of the values displayed in Table 1.

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, assumptions, and data may also be reasonable, and might produce different results.
5. We prepared this draft fiscal note for the Select Committee on Pension Policy.
6. We prepared this draft fiscal note and gave opinions 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 – ASSUMPTIONS WE MADE

We assumed no pre-retirement terminations or disablment. That is, we assumed that each member would reach retirement age. For members currently age 65 or older, we assumed they would retire immediately.

We calculated the deferred annuity factors using SERS Plan 2 mortality regardless of whether the member had previously resumed employment in PERS. We used the SERS assumptions for blending the annuity factors between male and female. In SERS we assume 55 percent of the population is female.

We assumed that all members would elect to transfer their eligible service from SERS back to PERS.

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

APPENDIX B – HOW WE APPLIED THESE ASSUMPTIONS

We used an individual annuity factor model to determine the liability associated with the service being transferred from SERS to PERS. The total liability being transferred equals the sum of the individual liabilities. We received the data used to calculate the liabilities and savings funds from DRS listing all the members with service transferred since September 1, 2000. For a description of the data please see Appendix C. For each member we determined their current age, their current total service and salary, and their projected service and age at retirement. From the original transfer to SERS the data included the number of months of service credit transferred, the savings fund, and the date of transfer.

We used the SERS salary inflation, salary merit, AFC calculation, and mortality assumptions described below to create the following factors:

- Pay Factor – based on the member's total current service earned to date. For non-vested members no longer employed in either PERS or SERS, we set this factor equal to one.
- Average Final Compensation (AFC) Factor – based on the member's projected service at retirement. For members no longer active in PERS or SERS we used a five-year AFC factor of 0.92; based solely on the SERS general salary increase assumption of 4.25 percent per year.
- Annuity Factors – deferred life-annuity factors with a 3 percent cost of living adjustment after the deferral period. We used factors deferred to ages 55 through 65 depending on the age and service combination of a given member.
- Present Value of Future Benefits (PVFB) Factor – calculated using the other factors as follows: (AFC Factor x Annuity Factor) / Pay Factor

The liability for each individual equals the product of their years of service transferred times the 2 percent plan accrual rate times their current salary times their calculated PVFB factor times an early retirement reduction factor.

Because DRS doesn't report salaries for TNV members, the calculation just described yields a liability of zero. We set their liability equal to the value of their transferred savings funds with interest accumulated to the valuation date.

For terminated vested members without a salary, we assigned them the SERS Plan 2 average salary from the 2007 AVR of $26,531.

The value of the assets transferred from SERS Plan 2 to PERS Plan 2 equals the sum of the individual member savings funds with interest. DRS reported the original savings fund values transferred to SERS from PERS in the data along with the dates the individual transfers took place. We applied the 5.5 percent interest rate, compounded quarterly, to determine the savings fund values as of the valuation date. DRS prepared the data file from after the valuation date; therefore, we discounted some of the members' savings funds back to the valuation date.

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

APPENDIX C – SPECIAL DATA NEEDED

Of the 5,799 records in the data file, we excluded 3,939 from this pricing for the following reasons:

- The member transferred to or from a Plan 3.
- The member had previous service in PERS in a SERS eligible position.
- The member didn't have any data in the PERS or SERS 2007 valuation data. This implies the member either terminated and withdrew their service, or transferred to a different system. In either case we didn't include these members because we could not accurately value their liability or savings funds.
- The member didn't have any months of service credit transferred, just the right to restore PERS service credit in SERS.

The following table summarizes the number of records excluded by cause. We identified some of the records as not being eligible for more than one reason; therefore, the "Total Count Excluded by Reason" in the table below totals to more than the 3,939 records excluded from this pricing.

Table 2

Summary Counts of Excluded Records by Cause of Exclusion

Reason for Exclusion	Total Count Excluded by Reason	Additional Records Excluded when Reasons are Taken in Order (top to bottom)
Member of a Plan 3	422	422
Prior PERS Educational Service	1,926	1,725
No data in any system	377	303
No months of service transferred	1,915	1,489
Total	**4,640**	**3,939**

Otherwise, we developed these costs using the same assets and data as disclosed in the 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 not covered by plan assets.