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.
- The Legislature has dealt with this before (1986 and 1991) and did not 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

- **Option 1: Refund Contributions For Non-credited Service.**
    - Does not require a retroactive policy change.
    - Consistent with past legislative actions in not retroactively changing service credit policy.
    - Less generous than granting service credit.
- **Option 2: 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.

❖ **Option 3: 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.

❖ **Option 4: Take No Action.**

- Generally consistent with approach taken by past legislatures.
- No cost impact.

Committee Activity

Staff briefed the Committee on this issue in June and October. In November, the Committee held a public hearing and took executive action recommending Option 3 to the Legislature.

Recommendation To 2009 Legislature

Grant half-time service to certain Plan 2/3 members who worked at least half-time for an educational employer prior to 1987.

Staff Contact

Darren Painter, Policy Analyst
360.786.6155
painter.darren@leg.wa.gov

O:\Reports\Interim Issues\2008\Exec_Summ\13.SERS_Past_PT_Svc_Cred_Exec_Sum.docx

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.

Darren Painter
Policy Analyst
360.786.6155
painter.darren@leg.wa.gov

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 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 provided 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).

**As of June, 2008.*

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.

Committee Activity

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

Staff briefed the 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.

The Committee held a public hearing and took executive action on this issue in November recommending Option 3 to the Legislature.

Executive Committee Recommendation

Option 3: Apply current half-time rules to past service. Recommended October 21, 2008.

Recommendation To 2009 Legislature

Grant half-time service to certain Plan 2/3 members who worked at least half-time for an educational employer prior to 1987. Recommended November 18, 2008.

Stakeholder Input

Correspondence on file from:

Carey Ensign, (e-mail and related attachment), 1/29/2008.

Bill Draft

A Code Reviser bill draft to implement the SCPP recommendation is attached (Z-0284.1/09).

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.

P:\Interim Issues-2008\FullReport\SERS_Past_PT_Svc_Credit_Issue_Paper.doc

BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #: Z-0284.1/09

ATTY/TYPIST: LL:lel

BRIEF DESCRIPTION: Granting half-time service credit for half-time educational employment prior to January 1, 1987, in plans 2 and 3 of the school employees' retirement system and the public employees' retirement system.

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

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

(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; and

(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 under the subchapter heading "provisions applicable to plan 2 and plan 3" 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 3 who is active in the retirement system and who earns service credit after the effective date of this section 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;

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

(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; and

(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**	**12/31/08**	**Z-0284.1 / Z-0404.11**

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.