

# Recommendation To PFC On Long-Term Economic Assumptions

## Issue

The state actuary is recommending changes to long-term economic assumptions for the state's retirement systems. The recommendation to the Pension Funding Council (PFC) and SCPP came out of a biennial review of economic experience required by statute. The SCPP has a statutory duty to make its own recommendation to the PFC regarding changes to economic assumptions.

## Background

Long-term economic assumptions are used for funding the state's retirement system and include investment return, salary growth, inflation, and membership growth. These assumptions are reviewed every two years according to a statutory cycle ([RCW 41.45.030](#)).

During odd-numbered years, the state actuary reviews economic assumptions and reports to the PFC and SCPP. The state actuary recommends any changes to the economic assumptions and reports on the experience and financial condition of the state's retirement systems. The PFC may adopt changes to economic assumptions subject to revision by the Legislature.

The SCPP has a statutory role in setting economic assumptions. Statute requires the committee to study changes to economic assumptions and make recommendations to the PFC ([RCW 41.04.281](#)).

The current economic assumptions are provided in the next section. The annual investment return assumption is scheduled in statute to decrease by 0.10 percent a biennium until reaching 7.7 percent in the 2017-19 Biennium.

## State Actuary's Recommendation To PFC

Assumption	Current	Recommended
Inflation	3.00%	3.00%
General salary growth	3.75%	3.75%
Annual investment return	7.90%	7.50%
Growth in system membership	0.80% (TRS) 0.95% (PERS)	0.80% (TRS) 0.95% (PERS)

*Note: Excludes LEOFF 2. The LEOFF 2 Board adopts assumptions for LEOFF 2.*

The state actuary further recommends lowering the assumption by extending the current statutory phase-in to the 2021-23 Biennium. Extending the phase-in would lower the assumption to 7.6 percent in the 2019-2021 Biennium and 7.5 percent in the 2021-23 Biennium.

More information on the state actuary's recommendation is provided in the attached materials.

## Options

### **Option 1: No Change To Current Assumptions**

This option would leave the current statutory assumptions unchanged. The current statutory phase-in will lower the investment return assumption to 7.7 percent by the 2017-19 Biennium. No fiscal impact.

### **Option 2: Extend Investment Return Assumption Phase-In**

This option would extend the current phase-in of the investment return assumption to the state actuary's recommended 7.5 percent. Extending the phase-in would lower the assumption to 7.6 percent in the 2019-21 Biennium and 7.5 percent in the 2021-23 Biennium. This option is the state actuary's recommended approach and is consistent with the SCPP's recommendation to the PFC in 2011.

Fiscal impacts would begin with the 2019-21 Biennium. This option would increase state general fund, total employer, and total employee costs by about \$50, \$140, and \$60 million in each of the 2019-21 and 2021-23 Biennia. These costs represent the average potential magnitude of the impact for each biennia. Short-term costs would continue beyond the biennia and ultimately become a long-term savings. More information on the fiscal impacts is provided in the attached PowerPoint.

### **Option 3: Adopt Lower Investment Return Assumption**

This option would lower the investment return assumption to the state actuary's recommended 7.5 percent without further phase-in. This would decrease the assumption from 7.8 percent to 7.5 percent in the 2015-17 Biennium.

Fiscal impacts would begin with the 2015-17 Biennium. This option would increase state general fund, total employer, and total employee costs by about \$140, \$400, and \$190 million. These costs represent the potential magnitude of the impact for the specified biennium only. Short-term costs would continue beyond the biennium and ultimately become a long-term savings. More information on the fiscal impacts is provided in the attached PowerPoint.

## Committee Activity

The SCPP received a briefing on the state actuary's recommended changes to long-term economic assumptions at the September meeting. The SCPP's recommendation to the PFC is scheduled for a public hearing and possible action at the October meeting.

## Additional Materials

- ❖ PowerPoint: State Actuary's Recommendations on Long-Term Economic Assumptions.\*
- ❖ 2013 Combined Reports on Financial Condition and Long-Term Economic Assumptions.\*
- ❖ Handout 1: History Of Economic Assumptions For Washington State Pension Systems
- ❖ Handout 2: Economic Assumptions for Selected Public Plans Outside Washington

*\*Originally included in the September 17, 2013 SCPP materials.*

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