Actuary's Draft Fiscal Note For TRS 3 Member Rate Flexibility

SUMMARY OF RESULTS

This proposal removes the statutory provision that allows Plan 3 members of the Public Employees Retirement System (PERS), the Teachers Retirement System (TRS), and the School Employees Retirement System (SERS) to select a new contribution rate option each year for their Defined Contribution (DC) accounts.

We do not expect this proposal to have a fiscal impact on the Washington State Retirement Systems.

HIGHLIGHTS OF ACTUARIAL ANALYSIS

Under current administrative practice, only TRS Plan 3 members are allowed to exercise contribution rate flexibility, so there would be no practical effect to PERS or SERS from this proposal.

The removal of Plan 3 rate flexibility in TRS 3 could impact future plan choice and future retirement behavior. Changes in plan choice and retirement behavior can change plan costs in TRS 2/3. However, for the reasons provided in the draft fiscal note, we do not expect this proposal to change future behavior in these areas. Therefore, we expect no fiscal impact from this proposal.

See the remainder of this fiscal note for additional details on the summary and highlights presented here.

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WHAT IS THE PROPOSED CHANGE?

Summary Of Proposal

This proposal impacts the following systems:

- PERS Plans 3.
- TRS Plans 3.
- SERS Plans 3.

This proposal removes the statutory provision that allows members of Plan 3 of PERS, TRS, and SERS to select a new contribution rate option each year.

Assumed Effective Date: 90 days after session.

What Is The Current Situation?

New hires choosing Plan 3 of PERS, TRS, or SERS must choose a contribution rate option for their DC accounts. For members of PERS 3 and SERS 3, this selection is permanent. The only way for those members to change rate options is to change employers.

Members of TRS 3 can choose to change their contribution rate option in January of each year, by notifying their employer in writing.

The rate flexibility option was enacted in statute for PERS 3, TRS 3, and SERS 3 in 2003. However, the Department of Retirement Systems has not administered the provision for PERS 3 and SERS 3 due to conflict with the Internal Revenue Code (IRC). Only members of TRS 3 have been able to change their rate option each year.

The table below displays the DC rate options available to all Plan 3 members.

Rate Option	Total Rate
Option A *(Default)*	5.0%
Option B	
Until age 35	5.0%
Age 35 to 44	6.0%
Age 45 and up	7.5%
Option C	
Until age 35	6.0%
Age 35 to 44	7.5%
Age 45 and up	8.5%
Option D	7.0%
Option E	10.0%
Option F	15.0%

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Who Is Impacted And How?

We estimate this proposal could affect 51,489 active members of TRS Plan 3 through a change in plan provisions.

This proposal removes the rate flexibility option for Plan 3 members. Plan 3 members do not contribute to their employer-provided defined benefit. We do not expect employer contribution rates for Plan 3 members will change as a result of this proposal.

Please see the following section for further details.

Why This Proposal Has No Expected Cost

The removal of Plan 3 rate flexibility in TRS 3 could impact future plan choice and future retirement behavior. Changes in plan choice and retirement behavior can change plan costs in TRS 2/3. However, for the reasons provided below, we do not expect this proposal to change future behavior in these areas. Therefore, we expect no fiscal impact from this proposal.

Plan Choice

Arguably, the ability to change a Plan 3 member contribution rate each year could impact a member's decision to select Plan 3 over Plan 2 at hire. Changes in assumed plan choice for future members can change future costs in Plan 2/3. However, we do not believe rate flexibility is a key component for members electing to join Plan 3 over Plan 2. Based on historical data over the last ten years, we see that less than 5 percent of the current TRS 3 active members change their contribution rate each year. As a result, we do not expect this proposal to materially change future plan choice.

Please see **Appendix A** for more details on historical TRS 3 member rate changes.

Retirement Behavior

The inability to change Plan 3 member contribution rates could change the ultimate amount of money saved for retirement and lead to earlier or later Plan 3 retirements in the future. Changes in future retirement behavior can change future costs in Plan 2/3. However, we do not believe the removal of rate flexibility will lead to material changes in future retirement behavior because Plan 3 members have other tax-advantaged savings vehicles with rate flexibility (457 plans – deferred compensation plans – and 403(b) plans – tax sheltered annuities).

If this proposal leads to material changes in either future plan choice or future Plan 3 retirement behavior, a cost or savings could result from this proposal.

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ACTUARIAL RESULTS

How The Liabilities Changed

We do not expect the proposal will change the present value of future benefits payable so there is no expected impact on the actuarial funding of the affected plans due to liability changes.

How The Present Value of Future Salaries (PVFS) Changed

We do not expect the proposal will change the PVFS of the members so there is no expected impact on the actuarial funding of the affected plans due to PVFS changes.

How Contribution Rates Changed

We do not expect any impact to contribution rates as a result of this proposal.

How This Impacts Budgets And Employees

We do not expect a Budget Impact as a result of this proposal.

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 in the footer. We intend this draft fiscal note to be used by the Select Committee on Pension Policy during the 2013 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 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 fiscal note as a whole. Distribution of, or reliance on, only parts of this fiscal note could result in its misuse, and may mislead others.

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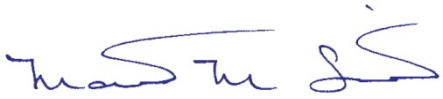
ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The assumptions used are appropriate for the purposes of this analysis.
2. We prepared this fiscal note for the Select Committee on Pension Policy during the 2013 Interim.
3. We prepared this draft fiscal note and provided opinions in accordance with Washington State law and accepted actuarial standards of practice as of the date shown in the footer of this fiscal note.

The undersigned, with actuarial credentials, meets the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

While this fiscal note is meant to be complete, the undersigned is available to provide extra advice and explanations as needed.



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Appendix A – Historical TRS 3 Member Rate Changes

Historical TRS 3 Member Rate Changes*				
Year of Rate Change	Contribution Rate Decreased	Contribution Rate Increased	Total Changes	Population (as of valuation date)
2004	1,138	3,135	4,273	49,302
2005	602	1,069	1,671	51,473
2006	654	1,245	1,899	53,371
2007	565	1,341	1,906	51,856
2008	585	1,348	1,933	52,360
2009	1,074	1,057	2,131	53,010
2010	729	1,038	1,767	52,292
2011	715	1,136	1,851	52,178
2012	659	934	1,593	51,489
Grand Total	6,721	12,303	19,024	467,331
			Total Change/Population	**4%**

**The counts for Employment Periods (EMSPs) that have more than one rate code*
The counts do not include members who separated and changed their contribution rate upon reemployment
Source: Department of Retirement Systems.

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