DRAFT Actuary's Fiscal Note For Z-0233.1/Z-0281.1

SUMMARY OF RESULTS

This proposal restores the general consistency between PERS return-to-work policies and most other state retirement systems. Specifically, it reapplies the 867-hour option to PERS retirees who return to work in positions covered by other state retirement systems and removes the 867-hour limit for PERS retirees who return to work in positions ineligible for state retirement system membership.

This proposal does not have a material cost to the state retirement systems.

HIGHLIGHTS OF ACTUARIAL ANALYSIS

This proposal may impact the retirement systems by changing retirement behavior.

The additional return-to-work restrictions currently in place for impacted PERS members could change their post-retirement income. Changes in income can, in turn, impact retirement behavior. For example, members might retire earlier if their income increases and might defer retirement if their income decreases. Based on this proposal, the easing of the extra restrictions could promote earlier retirement. Generally, when members retire earlier than expected, the result is an increase in costs to the retirement system.

However, we do not currently model the costs of the return-to-work program in any of our retirement systems because we do not expect they will materially impact contribution rates. Therefore, a minor adjustment to the immaterial costs would also be considered immaterial.

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

WHAT IS THE PROPOSED CHANGE?

Summary Of Change

This proposal impacts the following systems:

- Public Employees' Retirement System (PERS).

This proposal restores the general consistency between PERS return-to-work policies and most other state retirement systems. Specifically, it reapplies the 867-hour option to PERS Plan 2/3 retirees who return to work in positions covered by other state retirement systems and removes the 867-hour limit for PERS Plan 1/2/3 retirees who return to work in positions ineligible for state retirement system membership.

Effective Date: 90 days after session.

What Is The Current Situation?

Washington's return-to-work, or "retire-rehire" rules are complex and contain several exceptions. The following description only covers aspects of the return-to-work rules necessary to understand the changes made by Z-0233.1/Z-0281.1. For more information, please see the Department of Retirement Systems (DRS) publication *Thinking About Working After Retirement*.

Generally, the return-to-work rules allow an employee who separates from service and begins receiving his or her retirement benefits to return to work and continue receiving those retirement benefits. There are, however, limits on the amount of hours a retiree can work.

Typically, retirees are limited to working part time, up to 867 hours per year. If the retiree works longer, his or her retirement benefits will be temporarily suspended. In other words, the return-to-work rules do not prevent retirees from working as many hours as the retiree chooses, but instead limit how long the retiree can work each year *and continue receiving retirement benefit checks at the same time*.

These limitations do not apply if the retiree returns to work in the private sector, or works in a public job that is not otherwise eligible for state retirement system membership ("ineligible positions").

In 2011, the Legislature enacted ESHB 1981. That proposal changed several aspects of retirement statutes. Most of the changes in ESHB 1981 are not impacted by Z-0233.1/Z-0281.1.

Two of the changes in ESHB 1981 related to PERS return-to-work rules resulted in inconsistencies with other state retirement systems. These changes are addressed by Z-0233.1/Z-0281.1. Specifically:

- ESHB 1981 removed the 867-hour option for PERS Plan 2/3 retirees who return to work in other state retirement systems. PERS Plan 2/3 retirees who return to work would receive an immediate suspension of their benefits.
- ESHB 1981 applied an 867-hour limit to PERS retirees who return to work in positions ineligible for retirement benefits.

DRS reports that these two changes in ESHB 1981 are not currently being administered. Thus, Z-0233.1/Z-0281.1 is consistent with current practice.

Who Is Impacted And How?

We estimate this proposal could affect 152,417 active PERS members who may return to work in affected positions after they retire. We further estimate this proposal would affect the following members in the impacted PERS positions by increasing the number of hours they can work and receive retirement benefits compared to current law.

Members Impacted				
	PERS 1	PERS 2	PERS 3	All PERS
All Service Retirees (As Of June 30, 2011)	46,006	21,256	1,233	68,495
Returned to Work in Eligible Position Outside PERS*	N/A	109	4	113
Returned to Work in Ineligible Position*	3,365	1,127	56	4,548

**Information from Department of Retirement Systems as of November 2012.*

WHY THIS PROPOSAL DOES NOT HAVE A MATERIAL COST

Why This Proposal Does Not Have A Material Cost

While this proposal could theoretically increase retirement rates, thereby causing increased liabilities in PERS, we believe the costs would be immaterial. There are two potential sources of additional cost to the affected systems. Any costs that do occur would be absorbed by PERS as experience losses.

- PERS Plan 2/3 members who return to work in eligible positions in other state retirement systems, could work additional hours under this proposal and still receive their retirement benefits.
- Members of any PERS plan who return to work in ineligible positions could work unlimited hours under this proposal and continue to receive their retirement benefits.

Who Will Pay For These Costs?

Any costs that do occur as experience losses would materialize in future contribution rate increases payable according to the usual funding method for each plan.

- Plan 1 and Plan 3: 100 percent employer.
- Plan 2: 50 percent member and 50 percent employer.

HOW WE VALUED THESE COSTS

We based our analysis for this proposal on the same assets, data, assumptions, and methods as disclosed in the *June 30, 2011, Actuarial Valuation Report* (AVR).

We also relied on data from the Department of Retirement Systems to complete the **Who Is Impacted And How** section of this draft fiscal note. We relied on this data as complete and accurate. In our opinion, this information is adequate and substantially complete for purposes of this analysis.

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

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

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 2012 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.

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. 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 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 draft fiscal note is meant to be complete, the undersigned is available to provide additional advice and explanations as needed.

Lisa A. Won, ASA, FCA, MAAA
Actuary

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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 actuarial accrued liability. The normal cost is determined for the actuarial accrued 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 actuarial accrued 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) based on the PUC method.

Projected Benefits: Pension benefit amounts that 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.