



## Select Committee on Pension Policy

### Annuity Purchase

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### What's The Issue?

- Legislation passed in 2014 Session granting LEOFF 2 members option to purchase expanded annuity
- SCPP [correspondence](#) from Washington State Patrol Troopers Association requesting consideration for WSPRS members  
*"Our members are very active in Deferred Compensation, many from the very beginning of their employment, and the ability to use that money to purchase an annuity at the time of retirement in the WSPRS fund would be of great benefit. While keeping us consistent and competitive with other police agencies within the state."*
- Executive Committee expanded scope of review to include all plans



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**Key Policy Question**

- Should an expanded annuity purchase option be extended to all members of the state's retirement systems?



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**Today's Presentation**

- Background
- Policy highlights and fiscal considerations
- Next steps
- No action required



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## An Annuity Is A One-Time, Lump Sum Payment In Exchange For A Lifetime Fixed Monthly Payment

- Made at the time of retirement
- One-time payment is made for the remainder of retiree's life
- Investment performance does not impact fixed benefit payment
- Policy considerations differ in the context of Defined Contribution (DC) plans and Defined Benefit (DB) plans



## A DC Account Can Be Converted To An Annuity

- Provides guaranteed income for life, regardless of investment returns
- Only way to guarantee a member will not outlive their account balance
- A member is trading market risk and account growth for the guarantee of a steady income stream for life



## An Annuity Can Be Used To Supplement A DB Retirement Benefit

- Payment can come from a governmental savings plan roll-over (for example, 457 or 403(b) account) or other savings plan
- Annuity benefit can include same components and selections as normal retirement
  - COLA
  - Joint/survivor benefit



## There Are Similar Options Available To Some Members

- Five-year service credit purchase
  - Available to all retirement system members
  - Subject to return-to-work rules
- Annuity purchase for Plan 3 members
  - Available to all Plan 3 members
- Expanded annuity purchase
  - Available to TRS members and LEOFF Plan 2 members



## LEOFF 2 Legislation Passed During The 2014 Session

- Optional, one-time, lump sum, actuarially equivalent annuity purchase from the LEOFF Plan 2 trust fund
- Minimum purchase amount of \$25,000 rolled over from governmental plan
- If member dies, balance of purchase price is refunded to the beneficiary
- Retiree may rescind or alter the contract within 15 days of DRS receiving the contract



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## Approximately 209,000 Members May Be Impacted By Expanding An Annuity Purchase Option

- Less restrictive than the five-year service credit purchase option
- Creates benefit consistency across all plans
- Allows all members to benefit from WSIB performance and lower administrative costs
- Purchasing through the state results in lower costs for the member

	Interest Rate	Cost of Annuity
<b>Private Insurer</b>	4.0%	\$236,000
<b>DRS</b>	7.5%	\$157,000

Source: House Bill 2577 Actuarial Fiscal Note.  
Based on a LEOFF Plan 2 member age 56 buying a \$10,000 life annuity (including 3% COLA).  
For illustrative purposes only.

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## There Is No Expected Cost If All Assumptions Are Realized

- Primary assumptions impacting cost
  - Rate of investment return
  - Rate of mortality
  - Rate of inflation



## There Are Potential Risks

- Costs to the system
  - Longer lives
  - Lower investment returns
- Potential for anti-selection
  - Higher income members
  - Members with greater life expectancy
- Costs to the member
  - Lower inflation results in smaller COLA on annuitants benefit
- Possibly decades to realize any unfunded liabilities or surplus resulting from experience that differs from assumptions
  - Costs would be spread over remaining obligations of the plan



## The System Will Experience A Loss Or Gain If The Assumptions Do Not Match The Experience

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**Sensitivity Example – 56-Year-Old Purchases Retirement Annuity With \$100,000**

Scenario	Cash Paid From Member To Plan	Present Value of Plan Annuity	Cost to the Plan
1) Assumptions Realized	\$100,000	\$100,000	\$0
2) Members Living Longer Than Expected	\$100,000	\$102,558	\$2,558
3) Lower Asset Returns Than Expected	\$100,000	\$105,325	\$5,325
4) Scenarios 2 and 3	\$100,000	\$108,176	\$8,176

*Assumes annuity calculation based on 3% COLA and 90%/10% male/female mortality blend.*



## There May Be Ways To Mitigate Risks To The System

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- Set different assumptions to manage specific risks
- Adjustable benefit with a built in reserve to account for losses to the system
- Dedicated annuity fund



## Summary

- WSPTA requested consideration of expanding annuity purchase option to WSPRS to stay competitive with LEOFF Plan 2 counterparts
- All members have option of purchasing an additional five years of service credit; some also have option to purchase expanded annuity
- Expanding annuity purchase option to all members of the state's retirement systems
  - Creates benefit consistency
  - Allows all members to take advantage of state investment assumptions and administrative costs
  - Less restrictive than current options
- No expected costs if all assumptions are realized
- However, the system will experience loss/gains if experience differs from assumptions
- Should an expanded annuity purchase option be extended to all members of the state's retirement systems?



## Possible Next Steps

- No further action at this time
- Further study of the issue
- Draft legislation and update fiscal note

