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Impact of the State's 2021-23 Budget on TRS 1

The content of this document is also available on the Office of the State Actuary's website.

This information is intended to (1) document our understanding of the budget provision, (2) clarify how this is expected to impact the funding of the TRS 1, and (3) share our actuarial takeaways and related disclosures.

1. Summarized bill language:

   > Engrossed Substitute Senate Bill (ESSB) 5092 – **New Section 747 for the Teachers' Retirement System (TRS) Plan 1 Fund.**
   >
   > General Fund-State – $800,000,000.
   >
   > The appropriation is provided solely for expenditure on June 30, 2023, to the Unfunded Actuarial Accrued Liability (UAAL).

   We interpret this payment as an additional contribution to the plan, over and above the standard normal cost and UAAL rates collected over retirement system salaries. For purposes of this actuarial analysis, we assumed the Legislature will not modify the amount or timing of the payment as part of the 2022 or 2023 Sessions.

2. As of our *June 30, 2019, Actuarial Valuation Report* (AVR), the TRS 1 UAAL is $2,580 million. Not unlike a home mortgage, that obligation is expected to decline over time with payments towards interest and principal. Continuing the mortgage analogy, the $800 million payment in ESSB 5092 could be considered an extra payment towards the principal.

   This additional payment will increase future plan assets and correspondingly increase future plan funded status once deposited into the trust fund. As a result of making this additional $800 million payment, the **TRS 1 UAAL is expected to be fully funded approximately two years earlier** than previously anticipated (essentially moving up the estimated payoff year from 2026 to 2024).

   Please note, however, that future UAAL contribution rates will not be lower as a result of this payment since they are at the contribution rate floor established in statute – they'll just be paid for fewer years. The following table illustrates the contribution rates and budgetary impacts by funding source (a) under current law, (b) under this bill, and (c) the net difference.

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TRS Budget Impacts						
(a) Current Law						
(Dollars in Millions)	**2022**	**2023**	**2024**	**2025**	**2026**	**Total**
UAAL Contribution Rates	**6.19%**	**6.19%**	**6.19%**	**6.19%**	**6.19%**	
General Fund-State	$421	$440	$459	$480	$502	$2,302
Local Government	63	66	69	72	75	344
Total Employer	**$484**	**$506**	**$528**	**$552**	**$577**	**$2,646**
(b) ESSB 5092						
(Dollars in Millions)	**2022**	**2023**	**2024**	**2025**	**2026**	**Total**
UAAL Contribution Rates	**6.19%**	**6.19%**	**6.19%**	**0.00%**	**0.00%**	
General Fund-State	$421	$1,240*	$459	$0	$0	$2,121
Local Government	63	66	69	0	0	197
Total Employer	$484	$1,306	$528	$0	$0	**$2,318**
(c) Net Cost/(Savings)						
(Dollars in Millions)	**2022**	**2023**	**2024**	**2025**	**2026**	**Total**
UAAL Contribution Rates	**0.00%**	**0.00%**	**0.00%**	**(6.19%)**	**(6.19%)**	
General Fund-State	$0	$800	$0	($480)	($502)	($182)
Local Government	0	0	0	(72)	(75)	(147)
Total Employer	$0	$800	$0	($552)	($577)	**($328)**

**The General Fund-State cost in 2023 includes the $800M payment.*
Note: We use long-term assumptions to produce our short-term budget impacts. Therefore, our short-term budget impacts will likely vary from estimates produced from other short-term budget models.

Overall, this bill results in a net savings to employers and the General Fund-State. We assumed that funding for the standard TRS 1 UAAL contributions would be split 87 percent State and 13 percent Local Government. There's no impact to contribution rates paid by employees as a result of this bill.

For purposes of this analysis, we assumed that the supplemental UAAL contribution rates for the recent ad-hoc cost-of-living adjustments would shut off at the time the plan is fully funded and prior to being collected for the full ten years (as required for Plan 1 benefit improvements). Otherwise, we relied on our 2019 AVR and our Projections Disclosures to prepare this estimate.

3. In terms of risk, the $800 million payment (once made) is expected to improve both Affordability and Solvency Measures as defined on our Risk Assessment webpage. Separately, the actual TRS 1 payoff year may be earlier or later than calculated in this analysis depending on future events. In particular, the extent to which actual investment returns meet the statutorily assumed rate of 7.5 percent. In addition, if a UAAL re-emerges in the future, current funding policy would require UAAL contributions in an amount equal to or greater than the minimum rate in statute. Depending on actual experience, this could occur as soon as a year after the plan reaches full funding.

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We caution that **these estimates could change** with updated results and actual investment returns over the next couple years. More specifically, these estimates will become outdated with new actuarial valuations **starting in the Fall of 2021**. Please refer to those reports and our updated projections for more current analysis when available.

Note that our Projections Model includes actuarial data, assumptions, and methods consistent with our 2019 AVR, as well as actual investment returns through June 30, 2020. The analysis is **deterministic** in nature, meaning it assumes the trust fund will earn the statutorily assumed 7.5 percent investment rate of return each year in the future along with all other economic and demographic assumptions materializing as expected.

We prepared this analysis to assist interested stakeholders in evaluating this change to plan funding. We believe the set of actuarial assumptions, methods, and data used are reasonable given the purpose of this analysis; use of another set may also be reasonable and might produce different results. Our comments on risk involve the interpretation of many factors and the application of professional judgment.

The analysis of this bill provision does not consider any other changes to the systems; the combined effect of several changes to the systems could exceed the sum of each change considered individually. Please read the analysis shown herein as a whole; distribution of, or reliance on, only parts of this analysis could result in its misuse and may mislead others. We prepared this analysis and provided opinions in accordance with Washington State law and accepted Actuarial Standards of Practice as of May 2021, the publication date of this webpage.

We advise readers of this webpage to seek professional guidance as to its content and interpretation, and not to rely upon this communication without such guidance. ***Michael T. Harbour (ASA, MAAA)*** *meets the Qualification Standards of the American Academy of Actuaries; he served as the reviewing and responsible actuary for this analysis. While this communication is intended to be complete, he is available for any supplemental questions you may have by emailing State.Actuary@leg.wa.gov.*