SUMMARY OF RESULTS

BRIEF SUMMARY OF BILL: For all eligible PERS 1 and TRS 1 annuitants, this proposal enacts a one-time, permanent benefit increase of 3 percent on their first $44,000 of annual pension income (i.e., $110 per month cap).

COST SUMMARY

Impact on Contribution Rates *(Effective 9/1/2022)*				
	PERS	TRS	SERS	PSERS
Plan 1 UAAL	0.14%	0.27%	0.14%	0.14%

Consistent with RCW 41.45.070, PERS, TRS, SERS, and PSERS, employers will fund the cost of this benefit improvement through a supplemental contribution rate starting September 1, 2022, and collected over a ten-year period. There is no impact to employee rates as a result of this bill.

Budget Impacts			
(Dollars in Millions)	2022-2023	2023-2025	10-Year
General Fund-State	$21.2	$54.1	$304.6
Local Government	$11.5	$29.1	$160.5
Total Employer	**$37.2**	**$94.5**	**$526.8**

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.

HIGHLIGHTS OF ACTUARIAL ANALYSIS

- This bill results in a cost to the retirement systems and an increase to the UAAL. Larger benefits would be provided to eligible PERS 1 and TRS 1 annuitants than under current law, and these benefits were not anticipated or funded during impacted members' careers.
- Approximately 70 percent of PERS 1 annuitants and 90 percent of TRS 1 annuitants are expected to receive a benefit increase under this bill. Of those eligible, approximately 85 percent will receive a 3 percent increase in benefits, while the remaining 15 percent will receive the $110 per month cap. Annuitants not expected to receive a benefit increase are those currently receiving a COLA as part of the Basic or Alternate Minimum benefit. Please see **Who Is Impacted and How** for estimated impacted headcounts.
- This bill is expected to:
  - Increase PERS 1 UAAL by $177 million (5 percent increase) and TRS 1 UAAL by $169 million (7 percent increase) on a present value basis.
  - Immediately decrease the PERS 1 and TRS 1 funded ratios by 1 percent each.
- The TRS and PERS Plans 1 UAAL is currently expected to be paid off in 2023 and 2025, respectively. For the purposes of this fiscal note, we assume the supplemental rate calculated under this bill would be collected for a full 10-year period, regardless of the projected UAAL payoff dates.

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

WHAT IS THE PROPOSED CHANGE?

Summary of Bill

This bill impacts the following systems:

- Public Employees' Retirement System (PERS).
- Teachers' Retirement System (TRS).
- School Employees' Retirement System (SERS).
- Public Safety Employees' Retirement System (PSERS).

This bill provides retirees in PERS and TRS Plans 1 with a 3 percent increase in benefits (up to a maximum increase of $110 per month) beginning July 1, 2022. To be eligible, retirees must already be receiving a monthly benefit on July 1, 2021. Annuitants receiving Basic Minimum, Alternate Minimum, or temporary disability benefits are not eligible for the benefit increase under this bill.

Effective Date: July 1, 2022.

In this summary, we only include changes pertinent to our actuarial fiscal note. See the legislative bill report for a complete summary of the bill.

What Is the Current Situation?

Before it was repealed in 2011, the primary Cost-Of-Living Adjustment (COLA) provided in the Plans 1 was the Uniform COLA (UCOLA). The UCOLA was a fixed dollar amount multiplied by the member's total Years Of Service (YOS) and increased annually by 3 percent every July 1. The UCOLA was payable on the first calendar year in which the recipient turned age 66 and had been retired for one year. By July 1, 2010, the UCOLA was $1.88 per month/per YOS. This amounted to an annual increase of $677 for a recipient with 30 YOS.

Statute specified that future increases to the UCOLA were not a contractual right and the Legislature exercised the option to discontinue the UCOLA for most plan members during the 2011 Legislative Session.

Currently, the PERS and TRS Plans 1 provide automatic COLAs under two types of minimum retirement benefits only: The Basic Minimum and the Alternate Minimum.

The Basic Minimum is a fixed dollar amount per month multiplied by the member's total YOS and increases on July 1 every year by the dollar amount of the UCOLA. The Basic Minimum is currently $67.49*. If a member's benefit falls below this amount, they receive the UCOLA annual increase, which is $2.61/month per YOS as of July 1, 2021.

The Alternate Minimum is a fixed dollar amount per month (currently $2,076.34*) that increases by 3 percent each year. Eligible members must have at least:

- 20 YOS and be retired for at least 25 years, or

- ❖ 25 YOS and be retired for at least 20 years.

An optional Consumer Price Index (CPI)-based COLA is available to the Plans 1 members who elect it at retirement. The optional COLA was first made available in 1990 and provides an annual percentage increase in the retirement allowance. The increase is based on changes in the CPI for Urban Wage Earners and Clerical Workers for the Seattle area, up to a maximum of 3 percent per year. The optional COLA begins one year after retirement—regardless of age or service—and is in addition to any other COLAs received. Members who elect the optional COLA receive an actuarially reduced retirement allowance to offset the expected cost of the COLA over their lifetime.

In the 2018 Legislative Session, the Legislature passed Senate Substitute Bill (SSB) 6340 (Chapter 151, Laws of 2018), which provided a 1.5 percent COLA capped at $62.50 per month for Plans 1 members not receiving a minimum benefit who had been retired for a year as of July 1, 2018. This one-time COLA went into effect on July 1, 2018.

In the 2020 Legislative Session, the Legislature passed Engrossed House Bill (EHB) 1390 (Chapter 329, Laws of 2020) which provided a 3 percent COLA capped at $62.50 per month for Plans 1 members not receiving a minimum benefit who had been retired for a year as of July 1, 2020. This one-time COLA went into effect on July 1, 2020.

**Note as of July 1, 2021: The Alternate and Basic Minimum amounts are adjusted if the member elects voluntary payment options upon retirement. Throughout this fiscal note, we refer to the Basic and Alternate Minimum amounts prior to any voluntary reductions.*

Who Is Impacted and How?

As of June 30, 2019, we expect this bill would increase the retirement benefits for approximately 60,700 out of the total 78,200 PERS 1 and TRS 1 annuitants (78 percent) who are not receiving Basic Minimum or Alternate Minimum benefits.

This bill will increase the benefits for a typical annuitant by providing a one-time COLA during retirement. The table below shows the number of annuitants expected to receive the full 3 percent increase and the $110 per month cap. Most eligible annuitants are expected to receive a 3 percent COLA on their entire pension benefit. Annuitants receiving more than approximately $3,670 per month ($44,000 per year) would receive the $110 per month cap.

Estimated Headcounts as of June 30, 2019		
	PERS 1	TRS 1
Total Annuitants	45,600	32,600
Annuitants Not Receiving Minimum Benefit	32,000	28,700
Annuitants to Receive 3.0% COLA	26,700	25,800
Annuitants to Receive $110 Per Month Cap	5,300	2,900

This bill impacts all PERS, TRS, SERS, and PSERS employers through increased Unfunded Actuarial Accrued Liability (UAAL) contribution rates. This bill will not affect member contribution rates.

WHY THIS BILL HAS A COST AND WHO PAYS FOR IT

Why This Bill Has a Cost

This bill has a cost because it provides larger benefits for eligible PERS and TRS Plans 1 annuitants than the benefits provided under current law.

Who Will Pay for These Costs?

The costs that result from this bill will be paid by employers of PERS, TRS, SERS, and PSERS according to the standard funding method. PERS, SERS, and PSERS employers make PERS 1 UAAL payments, whereas TRS employers make TRS 1 UAAL payments.

HOW WE VALUED THESE COSTS

We modeled the current law cost of the retirement systems using our most recent actuarial valuation report (*June 30, 2020, Actuarial Valuation Report*) and assumptions and methods found on our projections webpage. We also reflected the economic assumptions adopted by the Pension Funding Council during the 2021 Interim. This set of assumptions, methods, and data form our new "base model".

To analyze the impact of this bill, we then adjusted the following assumptions, methods, or data used in the base model.

Assumptions We Made

In addition to the "base model" assumptions, we also made an adjustment for assumed demographic changes from the valuation date, June 30, 2019, to the effective date of this bill, July 1, 2022. Based on projections of the 2019 AVR, which account for expected mortality and new retirements, and our professional judgment, we estimate the total annuitant population on July 1, 2022, will be approximately 6 percent smaller in both PERS 1 and TRS 1.

How We Applied These Assumptions

The fiscal impact of this bill represents the change in projected contributions. To estimate the fiscal impact of this bill, we compared projected pension contributions under current law to the projected contributions we expect under this bill. The projected pension contributions reflect contributions from the current members as well as future hires.

To determine the projected costs under this bill, we modified the programming to reflect the increased benefits from the one-time COLA under this bill. We adjusted our valuation such that all currently retired members not already receiving a COLA through the Basic or Alternate Minimum monthly benefit, receive a one-time 3 percent COLA subject to a $110 monthly cap. We then multiplied the respective new contribution rates reflecting these changes by future payroll.

To reflect the impact of assumed demographic changes to the Plans 1 populations, we reduced the liability impact from this bill by 6 percent for both plans.

Lastly, we amortized the cost of this benefit improvement over a fixed ten-year period, consistent with PERS and TRS Plan 1 funding policy for benefit improvements.

Otherwise, we developed these costs using the same methods as our "base model."

Special Data Needed

There was no special data needed for this pricing.

ACTUARIAL RESULTS

How the Liabilities Changed

This bill will impact the actuarial funding of PERS 1 and TRS 1 by increasing the present value of future benefits payable to the members. The impact of the increasing present value of future benefits payable for current members is shown below.

Impact on Pension Liability			
(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits *(The Value of the Total Commitment to All Current Members)*			
PERS 1	$11,575	$176.7	$11,752
TRS 1	$8,415	$168.8	$8,584
Unfunded Actuarial Accrued Liability *(The Portion of the Plan 1 Liability That Is Amortized According to Funding Policy)**			
PERS 1	$3,759	$176.7	$3,936
TRS 1	$2,580	$168.8	$2,749
Unfunded Entry Age Accrued Liability *(The Value of the Total Commitment to All Current Members Attributable to Past Service That Is Not Covered by Current Assets)*			
PERS 1	$4,074	$176.7	$4,250
TRS 1	$2,847	$168.8	$3,016

Note: Totals may not agree due to rounding.
**PERS 1 and TRS 1 are amortized over a ten-year period.*

How the Assets Changed

This bill does not change asset values so there is no impact on the actuarial funding of the affected plans due to asset changes.

How the Present Value of Future Salaries (PVFS) Changed

This bill does not change the PVFS so there is no impact on the actuarial funding of the affected plans due to PVFS changes.

How Contribution Rates Changed

The rounded increase in the required actuarial contribution rate results in the supplemental contribution rate shown on page one that applies in the current biennium. This fixed rate is expected to be collected for a ten-year period consistent with how benefit improvements are funded in PERS 1 and TRS 1 under the Revised Code of Washington (RCW) 41.45.070.

Impact on Contribution Rates *(Effective 9/1/2022)*

System/Plan	PERS	TRS	SERS	PSERS
Current Members				
Employee (Plan 2)	0.00%	0.00%	0.00%	0.00%
Employer				
Normal Cost	0.00%	0.00%	0.00%	0.00%
Plan 1 UAAL	0.14%	0.27%	0.14%	0.04%
Total	**0.14%**	**0.27%**	**0.14%**	**0.14%**
New Entrants*				
Employee (Plan 2)	0.00%	0.00%	0.00%	0.00%
Employer				
Normal Cost	0.00%	0.00%	0.00%	0.00%
Plan 1 UAAL	0.14%	0.27%	0.14%	0.14%
Total	**0.14%**	**0.27%**	**0.14%**	**0.14%**

**Rate change applied to future new entrant payroll and used to determine budget impacts only. Current members and new entrants pay the same contribution rate.*

How This Impacts Budgets and Employees

Budget Impacts					
(Dollars in Millions)	**PERS**	**TRS**	**SERS**	**PSERS**	**Total**
2022-2023					
General Fund	$3.0	$16.0	$1.9	$0.4	$21.2
Non-General Fund	4.4	0.0	0.0	0.1	4.5
Total State	**$7.4**	**$16.0**	**$1.9**	**$0.5**	**$25.7**
Local Government	7.4	2.4	1.4	0.3	11.5
Total Employer	**$14.8**	**$18.4**	**$3.3**	**$0.8**	**$37.2**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2023-2025					
General Fund	$7.4	$41.0	$4.7	$1.1	$54.1
Non-General Fund	11.1	0.0	0.0	0.1	11.3
Total State	**$18.5**	**$41.0**	**$4.7**	**$1.2**	**$65.4**
Local Government	18.5	6.1	3.5	0.9	29.1
Total Employer	**$37.0**	**$47.1**	**$8.2**	**$2.1**	**$94.5**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**
2022-2032					
General Fund	$40.5	$232.1	$25.6	$6.4	$304.6
Non-General Fund	60.8	0.0	0.0	0.9	61.6
Total State	**$101.3**	**$232.1**	**$25.6**	**$7.3**	**$366.3**
Local Government	101.3	34.7	19.3	5.3	160.5
Total Employer	**$202.5**	**$266.8**	**$44.8**	**$12.6**	**$526.8**
Total Employee	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**

Note: Totals may not agree due to rounding. 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.

The analysis of this bill 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.

Comments on Risk

Similar to SSB 6340 passed in 2018 and EHB 1390 passed in the 2020 Session, this bill provides a one-time, permanent increase in benefits for eligible annuitants. If the Legislature develops a repeated pattern of providing similar ad hoc COLAs in the future, it could have a significant impact to short-term budgets, projected Plan 1 pay-off dates, and the pension risk measures.

If this bill were to pass, the Office of the State Actuary may be required to reflect an assumption of future COLAs when preparing the financial reporting under the Government Accounting Standards Board requirements. While this change will have no contribution rate or short-term budget impacts, it could result in the total pension liability (TPL) for PERS and TRS Plans 1 increasing by approximately 5 to 8 percent. The actual impact to the TPL could be more or less than shown.

Our office performs annual risk assessments to help us demonstrate and assess the effect of unexpected experience on pension plans. The risk assessment allows us to measure how affordability and funded status can change if investment experience, expected state revenue growth, and inflation do not match our long-term assumptions. Our annual risk assessment also considers past practices, for funding and benefit enhancements, and their impact on pension plan risk if those practices continue.

The following table displays our latest risk measurements as of June 30, 2020. The figures in this table were not reproduced for this bill. For more information, please see our Risk Assessment, Commentary on Risk, and Glossary webpages. Additional information on the assumptions used to produce the risk measures can be found in the *Risk Assessment Assumptions Study.*

Select Measures of Pension Risk as of June 30, 2020	FY 2021-39	FY 2040-69
Affordability Measures		
Chance of Pensions Double their Current Share of GF-S*	<1%	1%
Chance of Pensions Half their Current Share of GF-S*	65%	52%
Solvency Measures		
Chance of PERS 1, TRS 1 in Pay-Go**	1%	7%
Chance of Open Plan in Pay-Go**	<1%	1%
Chance of PERS 1, TRS 1 Total Funded Status Below 60%	7%	7%
Chance of Open Plans Total Funded Status Below 60%	17%	27%

**Pensions approximately 5.9% of current GF-S budget; does not include higher education.*
***When today's value of annual pay-go cost exceeds $50 million.*

Increasing PERS 1 and TRS 1 annuitant benefits will increase the chance of those plans entering pay-go status as well as increase the required cost of benefits if the plan enters pay-go. We expect the short-term impact to funded status from this bill to be an immediate reduction of the PERS and TRS Plans 1 funded status by approximately 1 percent each.

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

The best estimate results can vary under a different set of assumptions. To determine the sensitivity of the actuarial results to the best estimate assumptions selected for this pricing we varied the following assumptions:

- Future Investment Return.
- Mortality.

If the plan realizes investment returns higher than the prescribed long-term assumption of 7 percent per year, then the costs of this bill will be less than the costs shared on page one of this fiscal note. Conversely, if the plan realizes investment returns lower than the prescribed long-term assumption of 7 percent per year, then the costs of this bill will be more expensive.

Similarly, if members of PERS 1 and TRS 1 live longer than expected (lower mortality), the costs of this bill will be more expensive than the costs shared on page one. Conversely, if members of PERS 1 and TRS 1 live shorter than expected (higher mortality), the costs of this bill will be less expensive.

If the liability increase from this bill is more or less than expected, it will be funded through higher/lower UAAL contributions as defined in RCW 41.45.010. This can occur up to and beyond the ten-year supplemental rate period as required. Under current law, neither the supplemental rate described on page one, nor for how long that supplemental rate is collected, will change if the liability increase from this bill is more or less than expected.

The table below outlines how the liability impacts attributable to this bill change when we assume the investment return is 1 percent lower or higher than the prescribed assumption.

Impact of Higher/Lower Assumed Returns on Pension Liability			
(Dollars in Millions)	**Higher 8%**	**Best Estimate 7%**	**Lower 6%**
PERS 1	$168	$177	$187
Percent Change from Best Estimate	(5%)		6%
TRS 1	$160	$169	$178
Percent Change from Best Estimate	(5%)		6%

Likewise, the table below outlines how the liability impacts attributable to this bill change when we assume higher or lower rates of future mortality than our best estimate for service retirees and beneficiaries. For higher mortality, we assumed members experience mortality as if they were one year older than their current age under our best estimate. Similarly, for lower mortality, we assumed members experience mortality as if they were one year younger.

Impact of Higher/Lower Assumed Mortality on Pension Liability			
(Dollars in Millions)	**Higher Mortality**	**Best Estimate**	**Lower Mortality**
PERS 1	$174	$177	$180
Percent Change from Best Estimate	(2%)		2%
TRS 1	$166	$169	$171
Percent Change from Best Estimate	(2%)		2%

To put these results into context, if future investments return 6 percent instead of 7 percent per year, the costs associated with this bill will increase by approximately $10 million for PERS 1 and TRS 1 on a present value basis. Therefore, the ten-year funding of the supplemental rate, under this example, would fall short of collecting the full cost of this bill and the remaining unfunded costs from this bill would be funded through higher UAAL contributions.

The two scenarios shown above are provided for illustrative purposes only. The actual cost of this bill may vary from our best estimate and may fall outside the range of cost identified in this section.

ACTUARY'S CERTIFICATION

The undersigned certifies that:

1. The actuarial assumptions, methods, and data used are reasonable for the purposes of this pricing exercise. The use of another set of assumptions, methods, and data may also be reasonable and might produce different results.
2. The risk analysis summarized in this Actuarial Fiscal Note (AFN) involves the interpretation of many factors and the application of professional judgment. We believe that the assumptions, methods, and data used in our risk assessment model are reasonable for the purposes of this pricing exercise. However, the use of another set of assumptions, methods, and data could also be reasonable and could produce different results.
3. We prepared this AFN based on our current understanding of the bill as of the date shown in the footer. If the bill or our understanding of the bill changes, the results of a future AFN based on those changes may vary from this AFN. Additionally, the results of this AFN may change after our next annual update of the underlying actuarial measurements.
4. We prepared this AFN 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 AFN.

We prepared this AFN to support legislative deliberations during the 2022 Legislative Session. This AFN may not be appropriate for other purposes.

We advise readers of this AFN to seek professional guidance as to its content and interpretation, and not to rely on this communication without such guidance. Please read the analysis shown in this AFN as a whole. Distribution of, or reliance on, only parts of this AFN could result in its misuse and may mislead others.

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

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

Luke Masselink

Luke Masselink, ASA, EA, MAAA
Senior Actuary

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