

Attachment 6: Attorney General of Washington



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MEMORANDUM

DATE: October 10, 2025

TO: The Select Committee on Pension Policy

FROM: Jesse D. Yoder, Assistant Attorney General
Counsel to the Select Committee on Pension Policy 

SUBJECT: **State Law Analysis for Report on Substitute Senate Bill 5085 and Substitute House Bill 2034**

The Legislature has directed the Select Committee on Pension Policy (the “Committee”) to study two bills introduced during the 2025-26 legislative session and to report on the tax, legal, actuarial, pension policy, and administrative implications of each bill by January 9, 2026. *See* Laws of 2025, ch. 242, § 107. The two bills are:

1. **Substitute Senate Bill 5085 (“SSB 5085”).** SSB 5085 proposes a merger of three of Washington’s closed retirement plans: the public employees’ retirement system plan 1 (“PERS 1”); the teachers’ retirement system plan 1 (“TRS 1”); and the law enforcement officers’ and firefighters’ retirement system plan 1 (“LEOFF 1” and, together with PERS 1 and TRS 1, the “Closed Plans”). The merger of the Closed Plans would result in a new legacy retirement system (“LRS”).
2. **Substitute House Bill 2034 (“SHB 2034”).** SHB 2034 proposes a termination and restatement of LEOFF 1, with all liabilities and certain assets of the plan transferred into a new restated plan (“Restated LEOFF”).

The Committee asked counsel to analyze SSB 5085 and SHB 2034 and provide a report to the Committee on the legal implications of these bills. This report covers the legal implications of these bills under Washington state law only. It is counsel’s understanding that Ice Miller LLP, in its capacity as Special Assistant Attorney General, has provided an analysis of the federal tax law implications of each bill.

This report is presented in three parts. The first is an executive summary of state pension law and related implications of each bill, along with recommendations for the Committee were they to recommend either bill to the Legislature. The second is background on the Closed Plans and brief descriptions of the proposals contained in each bill. The third provides a state law analysis with an overview of state pension law applicable to both bills, followed by issues specific to each bill. A summary of each bill is attached to this report as Appendix A.

ATTORNEY GENERAL OF WASHINGTON

Page 2

This report is intended to assist the Committee in responding to the Legislature's directive to prepare a report on SSB 5085 and SHB 2034. This report is my considered legal judgment as the Committee's assigned counsel and is not intended to be a formal opinion by the Attorney General.

I. EXECUTIVE SUMMARY

- Members of the Closed Plans have certain pension rights that are contractual in nature. Those rights can be found in Washington statutes and rules, and in Washington case law that interprets those statutes and rules.
- Members of the Closed Plans have a vested contractual right to a monthly service or disability retirement allowance that was guaranteed to them at the beginning of their service. This retirement benefit cannot be modified except under certain circumstances and to the advantage of the member.
- The monthly service or disability retirement allowances for members of the Closed Plans will not be reduced under SSB 5085 or SHB 2034. Therefore, the bills do not deny members of the Closed Plans their vested contractual right to a monthly retirement allowance.
- Members of the Closed Plans likely have a vested contractual right to the systematic funding of their retirement plan. To manage risk, I recommend that any proposal be supported by a study predicting the actuarial soundness of the proposal.
- Because SHB 2034 provides the resources necessary to meet present and future pension liabilities, LEOFF 1 members' vested contractual right to the systematic funding of their retirement plan to maintain its actuarial soundness is likely not violated by the termination and restatement proposal.
- The issue of distribution of any surplus assets is governed generally by federal law. However, state case law indicates that plan members are not entitled to any pension fund surplus.
- To the extent a fully-retired plan is required under federal law to terminate and restate a plan, SHB 2034 may not accomplish that goal. Additionally, I recommend that any proposal to the Legislature recommending SHB 2034 consider extending the authorization for transfers in section 505, revising section 106 to reserve rights as they existed prior to the enactment of the section instead of its effective date, and modifying or removing the statute of limitations in section 107 and the nonseverability clause in section 503.

ATTORNEY GENERAL OF WASHINGTON

Page 3

II. BACKGROUND

A. History and Benefits of the Closed Plans

Throughout the early twentieth century, retirement systems were created for the benefit of the state's public employees, teachers, law enforcement officers, and firefighters. Individual plans and systems began consolidating, first with the teachers' retirement fund in 1917, the PERS 1 predecessor in 1947, and LEOFF 1 in 1969. *See* Laws of 1917, ch. 163 (creating teachers' retirement fund); Laws of 1947, ch. 274 (creating state employees' retirement system); Laws of 1969, ch. 209 (creating LEOFF 1).

As further detailed in the Issue Paper of the LEOFF 1 Study, these early plans quickly proved to be underfunded. In 1976, the Legislature created the Department of Retirement Systems (DRS) to administer most of the state's retirement systems and the Office of the State Actuary (OSA) to provide actuarial expertise to the Legislature. Laws of 1976 2d ex.s., ch. 105, §§ 4, 19. The Closed Plans were then closed to new members on October 1, 1977. *See* Laws of 1977, ch. 293, § 1 (limiting TRS 1 to those employed on or before September 30, 1977); *see also* Laws of 1977, ch. 294, § 1 (closing LEOFF 1 to new members); Laws of 1977, ch. 295, § 1 (closing PERS 1 to new members).

As defined benefit plans, the Closed Plans offer their members a defined monthly allowance at retirement using different formulae based on: (i) years of service; (ii) a dollar amount derived from average salary/compensation; and (iii) a multiplier. *See* RCW 41.26.100 (detailing LEOFF 1 benefit formula); *see also* RCW 41.32.498 (TRS 1); RCW 41.40.185 (PERS 1). In addition, members of LEOFF 1 receive medical benefits paid by local government employers that are administered by local disability boards. RCW 41.26.110. These benefits include hospital stays, long-term care, and other non-reimbursed medical expenses that are determined as "necessary" by each member's local disability board. RCW 41.26.150(1). LEOFF 1 is also the only Washington state plan to include a fully-indexed cost-of-living-adjustment (COLA), meaning that each year members' benefits are adjusted for inflation without a cap on increases. RCW 41.26.240.

PERS 1 and TRS 1 do not include ongoing COLA provisions. Erosion of benefits due to inflation for PERS 1 and TRS 1 members has been addressed piecemeal by the Legislature, with several *ad-hoc*, limited COLAs and modest minimum benefit allowances. *See* RCW 41.32.485-4931 (providing for *ad-hoc* COLAs and minimum benefit allowances for TRS 1 members); RCW 41.40.197-1987 (PERS 1).

Due to several factors, LEOFF 1 became adequately funded to cover future liabilities with expected returns. *See* ISSUE PAPER at 8. In 2000, it was projected that contributions were no longer necessary and LEOFF 1 employers and active members were allowed to cease contributions entirely. *See* RCW 41.26.080(2). While no contributions have been made to the LEOFF 1 fund since, the Legislature authorized a one-time, lump-sum defined benefit on January 31, 2023, payable to retired LEOFF 1 members of \$100 per service credit month, while then-active members were offered the choice of a lump-sum or a tiered multiplier benefit at retirement. RCW 41.26.555.

ATTORNEY GENERAL OF WASHINGTON

Page 4

B. Proposal 1: SSB 5085 (Merger of the Closed Plans)

The first proposal, SSB 5085, provides a merger of PERS 1, TRS 1, and LEOFF 1 into a new legacy retirement system known as LRS. SSB 5085 § 201. Each of the Closed Plans would be fully closed, and the assets and liabilities of each plan would be transferred to the new LRS. *Id.* §§ 303(1)(b) (closing LEOFF 1), 303(2)(b) (closing TRS 1), 303(3)(b) (closing PERS 1), 303(6) (establishing a new LRS account in the state treasury).

Under LRS, members of the Closed Plans would be entitled to the same benefits from LRS as they held prior to the merger. *Id.* § 102. Specifically, Members of each Closed Plan would be placed into three benefit tiers named after the Closed Plans. *Id.* § 202. For example, members of the former TRS 1 plan would become members of and entitled to benefits from the teachers' retirement system plan 1 tier of LRS. *Id.* § 201(2)(b).

SSB 5085 also explicitly guarantees that members of the new LEOFF 1 tier of LRS would receive the same benefits as they would under current LEOFF 1, including survivor benefits and medical benefits paid by employers and administered by the local disability boards. *Id.* §§ 201(3)(b)-(c). Merger of the plans would not impact the functioning of the local disability boards and the boards and local government employers are instructed to continue administering benefits. *Id.* § 203. For members of TRS 1 and PERS 1, SSB 5085 also provides the benefit enhancement of an ongoing COLA, indexed to inflation with a cap of 3%, similar to the PERS 2 COLA currently in effect. *Id.* §§ 401-404; RCW 41.40.840.

To ensure compliance with federal tax law, SSB 5085 directs DRS to submit requests to the IRS for a determination letter regarding LRS's qualified status and a private letter ruling indicating there are no tax consequences for any LRS member. *Id.* § 301(2)-(3). In the event a determination letter states any conflict between SSB 5085 and plan qualification requirements under federal law that cannot be remedied by administrative or statutory changes, the PERS 1/TRS 1 COLA provisions expire the following June 30th and the remainder of the bill becomes null and void. *Id.* § 703(2)(b).

C. Proposal 2: SHB 2034 (Termination and Restatement of LEOFF 1)

The second proposal, SHB 2034, provides what it calls a termination and restatement of LEOFF 1 effective June 30, 2029. SHB 2034 § 102. The bill would establish the Restated LEOFF fund in the custody of the State Treasurer and transfer the amount necessary to satisfy 120% of projected benefits under LEOFF 1 as of the effective date. *Id.* § 104(1). The remaining funds in the current LEOFF 1 fund would be transferred to the pension funding stabilization account (the "PSFA"). *Id.* § 104(2). SHB 2034 amends current law to allow the Legislature to direct the state treasurer to make transfers from the PFSA to the general fund during the 2027-2029 biennium. *Id.* § 505 (amending RCW 41.45.230).

ATTORNEY GENERAL OF WASHINGTON

Page 5

To ensure a “fully retired plan,” SHB 2034 includes an optional additional benefit for *active*¹ members of LEOFF 1. SHB 2034 § 108. For members of LEOFF 1 who were actively employed on February 1, 2025, and remain employed would have the option to receive an additional five years of service credit and a one-time lump-sum benefit of \$25,000. *Id.* To receive the additional benefit, the active member would need to notify DRS by January 1, 2026, in writing, that they elect to enter retirement status immediately and irrevocably and to begin receiving benefits. *Id.*

The governing statutes of Restated LEOFF largely mirror those of the current LEOFF 1 plan. The bulk of the bill is a reproduction—with minimal modifications—of the current sections of chapter 41.26 RCW relevant to LEOFF 1 in a new chapter entitled “restated law enforcement officers’ and firefighters’ retirement system act.” SHB 2034 § 302. For example, the current section regarding LEOFF 1 members’ benefits at retirement is reproduced in its entirety, including a proviso that allows retired members to return to active service. *Id.* § 318; RCW 41.26.100. Specifically, current retired LEOFF 1 members who reenter employment “have the right to again retire at any time and his or her retirement allowance shall be recomputed, and paid, based upon additional service rendered and any change in final average salary.” RCW 41.26.100.

If enacted as currently drafted, SHB 2034 provides for direct review of any legal challenge to its operative sections by the Washington Supreme Court. SHB 2034 § 107. Any such challenges would need to be brought by June 30, 2027, and DRS is directed to mail notice of the act generally—and the statute of limitations specifically—to the last known address of each LEOFF 1 member or spousal survivor. *Id.*

Similar to SSB 5085, SHB 2034 includes direction to DRS to “seek appropriate guidance to ensure the continuous compliance” of LEOFF 1 and Restated LEOFF with federal tax law. SHB 2034 § 109. In the event the IRS formally concludes any legislative changes are necessary, those findings are to be promptly submitted to the Governor and the appropriate committees of the House of Representative and the Senate. *Id.* If required by federal law, any funds reverted to the State that must be reverted back, with interest. *Id.*

SHB 2034 also provides for a reservation of rights “without any diminution of the rights and benefits of the LEOFF plan 1 members, retirees, and surviving spouses, as they existed prior to the effective date of this section.” *Id.* § 106. Section 106, and every section except for sections 107-109 and 464, are effective June 30, 2029. *Id.* §§ 506-508. Sections 107-109 (which include the statute of limitations, optional additional benefit, and federal tax law provisions mentioned above) do not have an enumerated effective date and will be effective shortly after passage.

¹ As of June 30, 2024, there were six remaining active members in LEOFF 1. ISSUE PAPER at 5.

ATTORNEY GENERAL OF WASHINGTON

Page 6

III. STATE LAW ANALYSIS

A. Modification of Pension Plans

The Legislature has plenary authority to establish the terms of the public pension systems. The Legislature's power to enact laws "is unrestrained except when expressly or impliedly limited." *Luders v. City of Spokane*, 57 Wn.2d 162, 164, 356 P.2d 331 (1960). Washington courts have repeatedly stated that they will not substitute their judgment for the Legislature's with respect to the structure of public retirement plans. *Wash. Fed'n of State Emp. v. State*, 107 Wn. App. 241, 247, 26 P.3d 1003 (2001); *State Pub. Emp. Bd. v. Cook*, 88 Wn.2d 200, 206, 559 P.2d 991 (1977).

1. The Washington Constitution prohibits impairment of certain contract rights, and in pension cases courts apply the *Carlstrom* test informed by *Bakenhus*.

The principal restriction on the Legislature's authority to modify the public pension systems is the impairments clause of the Washington Constitution, which prohibits any law impairing the obligations of contracts. WASH. CONST. art. I, § 23 ("No bill of attainder, *ex post facto* law, or law impairing the obligations of contract shall ever be passed.").² This prohibition "is not an absolute one and is not to be read with literal exactness," and the Legislature is afforded some deference when impairing private contracts. *Wash. Fed'n State Emp. v. State*, 127 Wn.2d 544, 561, 901 P.2d 1028, 1036 (1995). However, "when a state impairs its own contract, courts apply more stringent review." *Wash. Educ. Ass'n v. Dep't Ret. Sys.*, 181 Wn.2d 233, 242, 332 P.3d 439 (2014) (WEA I).

Contractual pension rights were first recognized in the case of *Bakenhus v. City of Seattle*, 48 Wn.2d 695, 296 P.2d 536 (1956), where the Washington Supreme Court held that employees are entitled to a "substantial pension" and that pension rights "may be modified . . . only for the purpose of keeping the pension system flexible and maintaining its integrity." *Id.* 701. Modifications "must bear some material relation to the theory of a pension system and its successful operation," and any disadvantageous changes "should be accompanied by comparable new advantages." *Id.* at 702. Employees also have the right to "a retirement system actuarially designed through systematic funding to meet present and future liabilities." *Weaver v. Evans*, 80 Wn.2d 461, 478, 495 P.2d 639 (1972). These principles "have historically defined the analysis for impairment of public pension contracts in this state." *WEA I*, 181 Wn.2d at 243.

Independently from *Bakenhus*, a separate line of cases developed the analysis for impairment of other public contracts. See *Carlstrom v. State*, 103 Wn.2d 391, 694 P.2d 1 (1985). In *Carlstrom*, the Washington Supreme Court held that unconstitutional impairment occurs when the state

² The United States Constitution contains a similar prohibition. See U.S. CONST. art 1, § 10 ("No state shall . . . pass any . . . Law impairing the Obligation of Contracts."). The Washington Supreme Court has held that these provisions are "substantially the same and are to the same effect." *Ruano v. Spellman*, 81 Wn.2d 820, 825, 505 P.2d 447, 450 (1973); see also *Tyrpak v. Daniels*, 124 Wn.2d 146, 151, 874 P.2d 1374, 1377 (1994) (noting that the impairments clauses of the United States and Washington Constitutions "have [been] interpreted . . . to be coextensive.")

ATTORNEY GENERAL OF WASHINGTON

Page 7

substantially impairs an existing contractual right and the impairment is not “reasonable and necessary.” *Id.* 396. Subsequent cases divided the *Carlstrom* test into three parts: “(1) does a contractual relationship exist; (2) does the legislation substantially impair the contractual relationship; and (3) if there is substantial impairment, is it reasonable and necessary to serve a legitimate public purpose.” *Ret. Pub. Emp. Council v. Charles*, 148 Wn.2d 602, 624-25, 62 P.3d 470 (2003).

The Washington Supreme Court reconciled these analyses and held that, while *Bakenhus* informs the analysis in pension cases, “the *Carlstrom* public contract test applies with equal force to public pension contracts” and “forms the backbone of the analysis in pension cases.” *WEA I*, 181 Wn.2d at 243-244. Specifically, in *WEA I*, the court applied the *Carlstrom* test to the Legislature’s repeal of the uniform cost of living adjustment (“UCOLA”) in 2011. *Id.* The UCOLA was previously established by the Legislature in 1995, and authorized an increase in benefits to PERS 1 and TRS 1 that grew by an automatic three percent per year. Laws of 1995, ch. 345, §§ 2, 5. Importantly, the 1995 legislation included a reservation of rights clause that reserved the Legislature’s “right to amend or repeal this section in the future and no member or beneficiary has a contractual right to receive this postretirement adjustment not granted prior to that time.” *Id.* § 2(6). In the wake of the financial crisis, the Legislature exercised that right and repealed the UCOLA in 2011. Laws of 2011, ch. 362.

A class of PERS 1 and TRS 1 members brought suit claiming that, among other things, the 2011 repeal of the UCOLA violated the *Bakenhus* requirement that any disadvantageous changes must be accompanied by comparable new advantages. *WEA I*, 181 Wn.2d at 244. In rejecting this argument, the Washington Supreme Court applied the *Carlstrom* test, stating that even if a contractual right did exist (satisfying the first prong of the test), repeal of the UCOLA did not substantially impair that right. *Id.* *Bakenhus* informed the court’s analysis of the second prong, stating that “substantial impairment is measured by the implied consent and comparable new advantages analysis established in *Bakenhus* and its progeny.” *Id.* at 249. The court also upheld the reservation of rights clause as enforceable. *Id.*

2. Members of pension plans have a contractual right to the systematic funding of their plans to maintain actuarial soundness.

Members of pension plans in Washington have a contractual right “to a retirement system actuarially designed through systematic funding to meet present and future pension liabilities.” *Weaver v. Evans*, 80 Wn.2d 461, 478, 495 P.2d 639 (1972). The contours of this right have been developed in both *Weaver* and *Ret. Pub. Emp. Council v. Charles*, 148 Wn.2d 602, 625, 62 P.3d 470 (2003).

In *Weaver*, an appropriation of \$62 million was made by the Legislature to the teachers’ retirement system for the biennium ending June 30, 1971. *Weaver*, 80 Wn.2d at 463. This appropriation was to be paid in quarterly installments from the general fund, with the amounts distributed first to current pension payments, survivor benefits, and system expenses, with the balance credited to the pension reserve fund. *Id.* Toward the end of the biennium, the Governor sought to reserve the

ATTORNEY GENERAL OF WASHINGTON

Page 8

remaining \$18 million appropriation in order to balance the state's budget. *Id.* There were insufficient funds in the teachers' retirement fund for benefit payments through the end of the biennium, which required the board of trustees to transfer the shortfall from its reserve fund. *Id.* Mae Weaver, a retired teacher, sought a writ of mandamus to restore the funds reserved by the Governor. In granting the writ, the court found that the Legislature's longstanding practice of maintaining actuarial soundness had given rise to a contractual right, and that the Governor's actions unconstitutionally impaired that right. *Id.* at 478.

In *Charles*, the Legislature implemented an additional contribution rate reduction for employers in both PERS 1 and TRS 1 during the biennium ending June 30, 2001, after reducing those rates at the beginning of the biennium. *Charles*, 148 Wn.2d at 609. The plaintiffs challenged the second rate reduction as violating their right to the systematic funding of their plan, arguing the lower rates may impact the actuarial soundness of the plan. *Id.* at 617. The court found that the members' contractual right to the systematic funding of their plan to maintain its actuarial soundness was not impaired where there was no indication that the lower contribution rates would render the plan actuarially unsound. *Charles*, 148 Wn.2d at 484.

3. Members of a defined benefit pension plan do not have a contractual right to surplus assets.

Defined benefit pension plans guarantee members fixed periodic payments upon retirement. *See Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 439 (1999). Because members of a defined benefit plan are guaranteed a fixed payment, statutory benefits are not proportional to the contributions that employees pay into the plan. *See Wash. Fed'n State Emp.*, 107 Wn. App. at 245. The "employer bears the risk of investment and guarantees the distribution of the fixed benefit even if the value of the plan's investments decline." *Johnson v. City of Tacoma*, No. 74848-3-1, 2016 WL 3190548, *3 (Wash. Ct. App. June 6, 2016) (unpublished).

There are no statutes in Washington that describe the ownership of surplus assets in any of the pension systems. The Supreme Court of the United States has found that members of a defined benefit plan have no interest in the plan's surplus, observing:

Given the employer's obligation to make up any shortfall, no [defined benefit] plan member has a claim to any particular asset that composes a part of the plan's general asset pool. Instead, members have a right to a certain defined level of benefits, known as "accrued benefits." . . . [P]lan members generally have a nonforfeitable right only to their "accrued benefits," so that a plan's actual investment experience does not affect their statutory entitlement. Since a decline in the value of a plan's assets does not alter accrued benefits, members similarly have no entitlement to

ATTORNEY GENERAL OF WASHINGTON

Page 9

share in the plan's surplus — even if it is partially attributable to the investment growth of their contributions.

Hughes Aircraft, 525 U.S. at 440-441.³

B. Analysis of Proposal 1: SSB 5058 Merger Bill

1. SSB 5085 does not impair any of the members' contractual rights to benefits under the Closed Plans.

Of the pension benefits to which a member has a contractual right, the right to a retirement allowance provided for under statute is a clearly protected pension right. This was the right at issue in *Bakenhus*. *Bakenhus* involved the City of Seattle pension fund for police officers. At the beginning of the officers' employment, city ordinances provided future retirement allowances based on the salary attached to the officers' positions. During *Bakenhus*' employment as a police officer, the city enacted an ordinance that reduced police officers' retirement allowance by approximately one-third. *Bakenhus* claimed that the reduction of his benefit constituted an impairment of contract under section 23 of Article I of the Washington Constitution. The Washington Supreme Court agreed and found that an employee who accepts a job to which a pension plan is attached has contracted for a retirement allowance based on what was promised at the beginning of the employee's membership, and that the employee is entitled to receive that retirement allowance once the employee vests and retires. *Bakenhus*, 48 Wn.2d at 701.

Section 102 of SSB 5085 states that the Legislature "intends that this merger . . . be accomplished in a way that does not negatively impact benefits provided." SSB 5085 § 102. This intention is effectuated throughout the bill, making explicit guarantees that benefits to all members of the Closed Plans will not be negatively impacted. *See, e.g., id.* § 201(2)-(4) (transferring all liabilities of each Closed Plan to the LRS); *id.* § 203 (confirming the merger does not impact the functioning of the local disability boards or benefits paid under pre-LEOFF plans); *id.* § 204 (providing that the bill should be construed to avoid any unintended impacts to benefits); *id.* § 301(1) (instructing DRS to administer the bill in a way that does not negatively impact benefits).

Because of this language, it is a reasonable interpretation that SSB 5085 protects the retirement allowances of the members the Closed Plans and that, post-merger, each member's contractual right to the retirement allowance provided under the applicable existing plan will not be impaired.

In addition, SSB 5085 provides additional benefits to all members of the Closed Plans. The funding status for TRS 1 and PERS 1 would immediately improve, and the bill provides LEOFF 1 with the

³ *Hughes Aircraft* analyzed claims under the Employee Retirement Income Security Act of 1974 (ERISA), a federal law that is inapplicable to state public pension systems. Nevertheless, ERISA interpretation is sometimes used as guidance for the interpretation or analysis of general public pension concepts. In addition, the *Wash. Fed'n of State Emp. v. State* court and the *Johnson* court relied on *Hughes Aircraft* in their analyses of state and city public pension plans provisions.

ATTORNEY GENERAL OF WASHINGTON

Page 10

benefit of an ongoing funding source in the case of any future UAAL while exempting LEOFF employers from any future contributions. *See* SSB 5085 § 101(5). TRS 1 and PERS 1 members would also be provided the benefit enhancement of an ongoing COLA. SSB 5085 §§ 401-404.

2. Members of the Closed Plans have the right to the systematic funding of their pension plans to maintain the plans' actuarial soundness. That right is not impaired by SSB 5085.

Members have a right to the systematic funding of their pension fund to maintain the fund's actuarial soundness. *Weaver*, 80 Wn.2d at 495 P.2d 639 (1972), *Ret. Pub. Emp. Council v. Charles*, 148 Wn.2d 602, 62 P.3d 470 (2003). The question is whether the merger described in SSB 5085 negatively impacts the systematic funding of any of the Closed Plans. The answer is probably no.

In *Charles*, the Washington Supreme Court held that in the absence of proof that a statute or action of the Legislature impaired the actuarial soundness of a pension plan, members' right to the systematic funding of an actuarially sound system was not violated. *Charles*, 148 Wn.2d at 627. Here, there appears to be no evidence upon which a court could find that merging the pension funds of the Closed Plans under SSB 5085 will render the funds actuarially unsound. The court in *Charles* required proof that something more than the possibility of future harm will occur before finding that legislative action caused a pension fund to become actuarially unsound. *Id.* On the other hand, the *Weaver* court did not require proof of inability to pay current or future benefits, only that the Governor's actions undermined the Legislature's systematic funding program. *Weaver*, 80 Wn.2d at 478.

In the absence of proof that the merged plan would be actuarially unsound, SSB 5085 cannot be said to violate members' contractual right to an actuarially sound plan and systematic funding.

3. State law does not prohibit different pension plans from being merged.

As explained above, the terms of members' public pension rights are defined by the language of the statutes creating those rights. A review of the Closed Plans' statutes and other provisions governing public pension plans shows there is no state statute that addresses whether any of the Closed Plans may merge with another plan. Given (i) the statutory silence on merger, and (ii) the Legislature's plenary power to design the public pension plans, there is no apparent prohibition under state law to the merger of these two different pension plans.

SSB 5085 merges the assets and liabilities of a closed law enforcement officers' and firefighters' pension plan, a closed teachers' retirement plan, and a closed public employees' retirement plan. There is little precedence in Washington public pension history for the merger described in SSB 5085.

In 1969, law enforcement officers and firefighters were transferred into LEOFF 1 from their membership in retirement plans that were administered by local governments. *See* chapters 41.16, 41.18, and 41.20 RCW (the "Prior Acts"). However, unlike Senate Bill 6668, the transfer of Prior

ATTORNEY GENERAL OF WASHINGTON

Page 11

Act employees into LEOFF 1 did not require that the Prior Acts become tiers of LEOFF 1, and the transfers of members to LEOFF 1 did not require the merger of assets and liabilities with LEOFF 1. Therefore, the creation of LEOFF 1 does not provide guidance for the merger anticipated in SSB 5085.

In answering the question whether state law will allow a merger of two disparate plans we need to review two basic legal provisions applicable to Washington public pensions. The first is that members' contractual rights are defined by the language of the statute creating those rights. *WEA I*, 181 Wn.2d at 244-45. The second is that the "Legislature has plenary authority to establish the terms of the public pension systems." *Luders v. City of Spokane*, 57 Wn.2d 162, 164, 356 P.2d 331 (1960). The statutes governing the Closed Plans do not address issues of merger—either by permitting or by prohibiting mergers. While it is always a risk that a Washington court may invalidate a merger of the Closed Plans, it is not readily apparent upon what grounds a court would invalidate a merger under state law. This is especially true given the Washington Supreme Court's acknowledgment that the Legislature has plenary power to alter or amend retirement plans as long as the amendment passes muster under the Constitution's contracts clause. Further, courts have indicated they will not substitute their judgment for the Legislature's with respect to the structure of public pension plans. *Wash. State Pub. Emp. Bd. v. Cook*, 88 Wn.2d 200, 206-07, 559 P.2d 991 (1977). It is unlikely they would do so here.

4. LEOFF 1 members do not have a right to the surplus assets of their plan under state law. However, federal law will likely be dispositive on this issue.

The LEOFF Plan 1 pension fund currently has a surplus. The State Actuary notes that, based on assumptions as of June 30, 2024, LEOFF 1 has an expected surplus of \$2.5 billion. The LEOFF 1 surplus is intended to improve the actuarial soundness of TRS 1 and PERS 1 after the merger. *See* SSB § 102.

There is no provision in LEOFF 1 statute that addresses the ownership of surplus assets. Pursuant to RCW 41.26.020, members clearly have a right to a reserve system that pays them a retirement allowance but there does not appear to be any statutory provision that supports members' ownership of the surplus assets. Because members of a defined benefit plan do not share in the decrease or surplus of plan assets, under the reasoning of *Johnson v. City of Tacoma* and *Hughes Aircraft Co. v. Jacobson*, it seems unlikely that a court would find that LEOFF 1 members are entitled to the surplus assets of their plan. Further, SSB 5085 does not seek to distribute the surplus assets but, instead, to merge those assets with those of the other Closed Plans and create an expanded LRS asset pool.

Importantly, however, the Closed Plans have been determined to be a tax qualified plan under the federal Internal Revenue Code and must be administered consistent with federal law. This report defers to Ice Miller's analysis regarding SSB 5085 under federal tax law.

ATTORNEY GENERAL OF WASHINGTON

Page 12

C. Analysis of Proposal 2: SHB 2034 Termination and Restatement Bill

1. SHB 2034 does not impair LEOFF 1 members' contractual right to benefit payments or an actuarially sound plan.

As discussed in more detail above, an employee who accepts a job to which a pension plan is attached has contracted for a retirement allowance based on what was promised at the beginning of the employee's membership, and the employee is entitled to receive that retirement allowance once the employee vests and retires. *Bakenhus*, 48 Wn.2d at 701. To the extent Restated LEOFF benefits are identical to current LEOFF 1 benefits, SHB 2034 does not diminish any of the members' contractual rights to benefits.

Members of pension plans in Washington have a contractual right "to a retirement system actuarially designed through systematic funding to meet present and future pension liabilities." *Weaver*, 80 Wn.2d at 478. As discussed above, *Weaver* involved the Governor holding back funds the Legislature had appropriated for the teachers' retirement fund. *Id.* 463. This left the fund with a \$9.8 million shortfall and only \$37,224 in assets, forcing it to transfer funds from its reserve fund. *Id.* The court held that this impaired the members' "vested contractual rights to a retirement system actuarially designed through systematic funding to meet present and future pension liabilities." *Id.* 478.

In contrast, SHB 2034 provides ample funds to meet all present and future pension liabilities. The bill requires the transfer of enough funds to satisfy 120% of projected future liabilities under Restated LEOFF. SHB 2034 § 104(1). Additionally, unlike in *Weaver*, where the Governor redirected funds in direct opposition to the Legislature's careful direction, the funds here would be transferred to the general fund at the behest of the Legislature.

2. The optional benefit enhancement in SHB 2034 may not violate state law, but it also may not provide for a fully-retired plan.

Section 108 of SHB 2034 provides an optional additional benefit for members of LEOFF 1 who were actively employed on February 1, 2025, are still actively employed, and choose to irrevocably elect to enter retirement status by January 1, 2026. SHB 2034 § 108. The optional benefit would consist of a one-time lump-sum benefit of \$25,000 and an additional five years of service credit. As noted above, there were six remaining active LEOFF 1 members as of June 30, 2024.

There is precedent for one-time lump-sum benefit enhancements. *See* Laws of 2022, ch. 168 (LEOFF 1 lump-sum benefit). Members of plans are also able to accept the Legislature's offer to irrevocably waive certain pension benefits in exchange for others. *See Sloma v. Dep't Ret. Sys.*, 12 Wn. App.2d 602, 459 P.3d 396 (2020) (enforcing a PERS 1 member's irrevocable election into "post-30-year program").

While the Legislature may offer an optional additional benefit like the one in section 108, the benefit is ostensibly being made to ensure a "fully-retired plan" as of June 30, 2029. SHB 2034

ATTORNEY GENERAL OF WASHINGTON

Page 13

§ 108. However, SHB 2034 also restates current RCW 41.26.100 in its entirety, including the proviso that allows retired members to return to active service. SHB 2034 § 318 (providing that “the recipient of a retirement allowance who shall return to service . . . *shall be considered to have terminated his or her retirement status* and he or she shall immediately become a member of the retirement system with the status of membership he or she had as of the date of retirement.”) (emphasis added). This not only creates an apparent contradiction between the irrevocable election in section 108 and the mandatory language of section 318, but highlights the risk that a currently retired member may return to work prior to June 30, 2029, potentially undermining the plan’s “fully-retired status.”⁴

Finally, it appears that the optional additional benefit in section 108 may be inadvertently carved out of the reservation of rights. Section 106 reserves the right of the Legislature “to make such amendments and modifications as may be necessary . . . without any diminution of the rights and benefits of the LEOFF plan 1 members, retirees, and surviving spouses, as they existed prior to the effective date of this section.” Most of SHB 2034, including section 106, has an effective date of June 30, 2029. SHB § 506. Section 108 does not have an enumerated effective date and will be effective shortly after passage and prior to the effective date of section 106 and therefore outside the scope of the reservation of rights. If the Legislature intends to reserve its right to make amendments and modifications to all sections of SHB 2034, I recommend revising the language to provide for a reservation of rights “as they existed prior to the *enactment* date of this section.”

3. SHB 2034 contains additional concerns that would need to be considered and addressed prior to passage.

As currently drafted, SHB 2034 provides that the Legislature may direct the State Treasurer “to make transfers of moneys in the [PFSA] into the state general fund” during 2027-29 fiscal biennium. SHB 2034 § 505. However, the termination of LEOFF 1, creation of Restated LEOFF, and the transfer of funds to the PFSA do not occur until June 30, 2029. As noted by the State Investment Board, this means the transfer of funds from PFSA to the general fund must only occur on June 30, 2029. *See* LEOFF 1 STUDY, Attachment 4. The Legislature may wish to extend the authorization in section 505 to ensure a more reasonable timeframe for the effectuation of Restated LEOFF and to prevent inadvertently locking funds into the PFSA.

Separately, the statute of limitations in SHB 2034 may not be enforceable. Section 107 provides that “[a]ny claim filed challenging the validity of sections 101 through 108 of this act not filed before June 30, 2027, is forever barred, if not already barred by an otherwise applicable statute of limitations.” SHB 2034 § 107. If passed during the 2026 Legislative Session, SHB 2034 would likely be effective for a year or less before the June 30, 2027 bar. However, the termination of LEOFF 1 and creation of Restated LEOFF would not occur until June 30, 2029. SHB 2034 § 102, § 506.

⁴ There is nothing under state law that requires LEOFF 1 to be a fully-retired plan to carry out the provisions of SHB 2034. This report defers to Ice Miller on whether federal law requires a fully-retired plan and the impact a member returning to service would have on that status.

ATTORNEY GENERAL OF WASHINGTON

Page 14

The Legislature has the prerogative to enact statutes of limitations as part of its “constitutional power to enact a clear line of demarcation to fix a precise time period beyond which no remedy will be available.” *Rodriguez v. Niemeyer*, 23 Wn.App 398, 401, 595 P.2d 952 (1979). Absent section 107, the Washington Supreme Court has held that actions alleging a breach of a state employee’s pension rights are subject to the three-year statute of limitations contained in RCW 4.16.080. *Noah v. State*, 112 Wn.2d 841, 774 P.2d 516 (1989). The Legislature may increase or decrease applicable statutes of limitations insofar as it does not unreasonably limit the opportunity to enforce a right of action. *See Torkelson v. Roerick*, 24 Wn.App 877, 604 P.2d 1310 (1979) (upholding shortening statute of limitations); *see also Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 437 (1982) (noting that “[t]he State may erect reasonable procedural requirements for triggering the right to an adjudication [including] statutes of limitations.”).

The Washington Supreme Court has held that barring actions not filed within one year of a statute’s effective date are not unreasonable. *Hoko River Boom Co. v. Fairservice*, 69 Wn. 357, 125 P. 145 (1912). However, SHB 2034 not only sets a statute of limitations of approximately one year from effectiveness, it also bars any challenges to sections 101-106 of the bill a full two years *before* their effective date. SHB 2034 § 506 (setting the effective date of sections 101-106, among others, at June 30, 2029). While the need for “prompt and ultimate determination” of claims prior to enactment detailed in section 107 may be compelling, counsel has not been able to locate any instances where the Legislature has barred claims *prior* to enactment of the legislation giving rise to those claims. Whether a court would enforce such a bar would likely be a question of first impression under Washington law.

Members challenging the operative sections of SHB 2034 may also attempt to assert a takings claim under 42 U.S.C. § 1983. Congress did not specify a particular statute of limitations for § 1983 claims, but it “endorses the borrowing of state-law limitation provisions where doing so is consistent with federal law.” *Owens v. Okure*, 488 U.S. 235 (1989). Although courts borrow from state law when analyzing a § 1983 claim, federal courts have the power to toll statutes of limitations in appropriate circumstances. *See Johnson v. Ry. Express Agency, Inc.*, 421 U.S. 454, 465 (1975) (“[C]onsiderations of state law may be displaced where their application would be inconsistent with the federal policy underlying the cause of action under consideration.”); *see also Larson v. Snow College*, 189 F.Supp.2d 1286 (Utah 2000) (refusing to adopt a state statute shortening time for bringing suit under the ADA against certain state institutions to two years). Given the concerns above regarding timing, it is reasonable to expect that a court may disregard the time bar in section 107 when analyzing a claim under federal law.

Finally, any challenge to SHB 2034 as drafted would likely be able to succeed simply by invalidating section 107. Section 503 provides that invalidation of any of sections 101 through 108 would invalidate the entire act. SHB 2034 § 503 (“[s]ections 101 through 108 of this act are not severable, and if any provision of those sections is held invalid by a court of competent jurisdiction, this entire act is null and void.”). Thus, section 107 may ultimately undermine its purpose of finality and cause the unwinding of SHB 2034 years after the termination and restatement occurs.

ATTORNEY GENERAL OF WASHINGTON

Page 15

To the extent the Legislature wishes to retain section 107, I recommend considering the removal or modification of the nonseverability language in section 503.

IV. CONCLUSION

In conclusion, the above represents the analysis of the Committee's assigned counsel as to how Washington courts may analyze SSB 5085 and SHB 2034 if they were to pass. While, in general, the conclusion of this report is that the merger in SSB 5085 and the termination and restatement in SHB 2034 appear to meet the requirements protecting the constitutionally protected contractual rights of the affected members, there is always a risk that Washington courts may analyze a merger according to different principles. Nevertheless, the Legislature may wish to adhere closely to the framework developed by Washington courts regarding the legal analysis of public pension rights of public pension members.

ATTORNEY GENERAL OF WASHINGTON

Page 16

APPENDIX A

SSB 5085 (Merger of Closed Plans)

SSB 5085 Section(s)	Contents
Section 101	<u>Legislative Findings</u> - Outlines history and funding status of each plan - Finds merger of plans would immediately remedy funding issues, provide ongoing funding source of LEOFF 1 were any future UAALs to occur, and increase COLA parity across all three plans
Section 102	<u>Legislative Intent</u> - Outlines intended accomplishments of the bill, which include: - o LEOFF 1 benefits remain unchanged - o PERS 1 and TRS 1 benefits remain the same, with an additional ongoing COLA as a benefit improvement - o Merger is administered to be consistent with federal plan qualification requirements
Section 201	<u>Merger</u> - Merges assets, liabilities, and membership of LEOFF 1, PERS 1, and TRS 1 into new Legacy Retirement System (LRS) plan - § 201(3)(b) explicitly provides that medical benefit liabilities under LEOFF 1 remain liabilities of employers
Section 202	<u>Benefit Tiers</u> - Establishes three separate tiers for each of LEOFF 1, PERS 1, and TRS 1
Section 203	<u>Disability Boards and Pre-LEOFF Plans</u> - No provisions of the bill are meant to impact operation of LEOFF 1 disability boards or pre-LEOFF plans

ATTORNEY GENERAL OF WASHINGTON

Page 17

SSB 5085 Section(s)	Contents
Section 204	<u>No Benefit Alteration</u> - Clarifies that the bill is largely not meant to alter any benefits, and any unintentional substantive impacts should be construed to avoid such impacts
Section 301	<u>DRS Administration Instructions</u> - Instructs DRS to avoid negatively impacting benefits to members in administering the bill - Instructs DRS to request determination letter and private letter ruling from IRS
Sections 302-304	<u>Conforming amendments to chapter 41.50 RCW</u> - Amends DRS statute to provide for the closure of plans 1 and creation of LRP
Section 401-404	<u>PERS 1 and TRS 1 COLAs</u> - Provides initial 3% COLA for PERS 1 and TRS 1 members and subsequent ongoing COLAs indexed to Seattle CPI - Ongoing COLAs capped at 3%, with plans 2/3-style banking
Sections 501-510	<u>Conforming amendments to chapter 41.45 RCW</u> - Amends language regarding actuarial funding of the state retirement systems to include the new LRP - Also includes changes to UAAL rates made moot by passage of ESSB 5357
Sections 601-615	<u>Miscellaneous conforming amendments throughout the RCW</u> - Amends various sections of the RCW to provide for the removal of LEOFF 1, PERS 1, and TRS 1 and addition of LRP
Sections 616-620	<u>New sections regarding merger</u> - Adds new sections to applicable plan chapters referencing merger of each plan into LRP

ATTORNEY GENERAL OF WASHINGTON

Page 18

SSB 5085 Section(s)	Contents
Section 701	<u>New chapter</u> - Designates sections 201-204 as a new chapter in Title 41 RCW
Section 702	<u>Effective Dates</u> - Provides for effective dates, with sections 401-404 effective July 1, 2025, section 615 effective July 1, 2028, and the remainder effective September 1, 2027
Section 703	<u>IRS Plan Qualification</u> - Provides that, in the event of conflict with IRS plan qualification requirements, the PERS 1/TRS 1 COLA provisions will expire the following June 30th and the rest of the bill will be null and void

SHB 2034 (Restatement of LEOFF 1)

SHB 2034 Section(s)	Contents
Section 101	<u>Legislative Findings and Declaration</u> - Outlines history of LEOFF 1 funding and current overfunding - Determines that termination and restatement of LEOFF 1 is best solution to overfunding - Declares legislative intent to terminate and restate LEOFF 1 in accordance with federal tax law and state contract law principles
Section 102	<u>Restatement and Termination</u> - LEOFF 1 is restated and terminated effective June 30, 2029, with benefits continuing during transition
Section 103	<u>Establishment of Restated LEOFF Plan</u> - Establishes the “restated law enforcement officers’ and firefighters’ retirement system” - May be referred to as Restated LEOFF or LEOFF Plan 1

ATTORNEY GENERAL OF WASHINGTON

Page 19

SHB 2034 Section(s)	Contents
Section 104	<u>Establishment of Restated LEOFF Fund</u> - Creates Restated LEOFF fund in the custody of OST - Fund consists of assets transferred from LEOFF 1 - An amount equal to 120% of the current projected value of LEOFF 1 benefits as of June 30, 2029, shall be transferred into the new fund - PFC shall conduct an independent audit of OSA calculation - Remaining LEOFF 1 funds to be deposited in the PFSA and invested by SIB until otherwise directed by law
Section 105	<u>Investment of Funds</u> - Funds to be invested by SIB
Section 106	<u>Reservation of Rights</u> - Legislature reserves right to make amendments and modifications without diminishing the rights and benefits of LEOFF 1 members prior to termination and restatement
Section 107	<u>Statute of Limitations</u> - Any challenge to the validity of sections 101-108 must be brought by June 30, 2027 - Claims are subject to direct review by the Supreme Court of Washington
Section 108	<u>Active Member Retirement Incentive</u> - Active members may elect to receive an incentive (\$25,000 one-time lump sum and 5 years of additional service credit) in exchange for irrevocably enter annuitant status and begin receiving benefits - Does not require active members to discontinue employment - Only available to members active as of February 1, 2025, that have remained continuously employed since that time - Election must be made by January 1, 2026

ATTORNEY GENERAL OF WASHINGTON

Page 20

SHB 2034 Section(s)	Contents
Section 109	<u>IRS Compliance</u> - Directs DRS to seek “appropriate guidance” to ensure continuous compliance with federal tax requirements - Any conclusions from IRS that require legislative fixes must be communicated to the Governor and Legislature - Provides for reversion of any funds with interest if necessary to comply with IRS requirements
Sections 201-204	<u>Amendments to chapter 41.26 RCW</u> - Amendments to chapter 41.26 RCW removing LEOFF 1
Sections 301-348	<u>Restated LEOFF</u> - Restates provisions of currently existing LEOFF 1 in a new, separate chapter - Section 318 restates current RCW 41.26.100 in its entirety, including proviso allowing for return to active status upon reemployment with eligible employee
Section 401-471	<u>Conforming Amendments</u> - Provides for conforming amendments throughout the RCW
Section 501	<u>Repealer</u> - Repeals miscellaneous provisions
Section 502	<u>Savings clause</u> - Preserves any rights or liabilities under any of the provisions repealed by section 501 - Applies any existing DRS rules for LEOFF 1 to Restated LEOFF
Section 503	<u>Nonseverability</u>
Section 504	<u>New Chapter</u> - Sections 101-107, 109, and 301-348 constitute a new chapter under Title 41 RCW

ATTORNEY GENERAL OF WASHINGTON

Page 21

SHB 2034 Section(s)	Contents
Section 505	<u>PFSA Transfer Authorization</u> - Amends RCW 41.45.230 to allow the Legislature to direct a transfer of funds from the PFSA into the general fund during the 2027-2029 biennium
Section 506-508	<u>Effective Dates</u> - Except Sections 107-109 and 464, the act would take effect on June 30, 2029.