Select Committee on Pension Policy

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Regular Subgroup Meeting

Plan 1 Funding Method Subgroup

August 21, 2006

2:00 PM - 4:00 PM
House Hearing Room C
Olympia

AGENDA

2:00 PM	**(1)**	**Review of Questions** - Matt Smith, State Actuary
3:00 PM	**(2)**	**Preliminary Analysis and Options** - Matt Smith
3:30 PM	**(3)**	**Next Steps**
4:00 PM	**(4)**	**Adjourn**

Persons with disabilities needing auxiliary aids or services for purposes of attending or participating in Select Committee on Pension Policy meetings should call (360) 786-6140. TDD 1-800-635-9993.

***Elaine M. Banks**
TRS Retirees

Representative Barbara Bailey

Lois Clement
PERS Retirees

Representative Steve Conway

Representative Larry Crouse

Senator Karen Fraser

***Representative Bill Fromhold**, Vice-Chair

Leland A. Goeke
TRS and SERS Employers

Robert Keller
PERS Actives

***Sandra J. Matheson**, Director
Department of Retirement Systems

Corky Mattingly
PERS Employers

Doug Miller
PERS Employers

Victor Moore, Director
Office of Financial Management

Senator Joyce Mulliken

***Glenn Olson**
PERS Employers

***Senator Craig Pridemore**, Chair

Diane Rae
TRS Actives

***J. Pat Thompson**
PERS Actives

Senator Mark Schoesler

David Westberg
SERS Actives

*** Executive Committee**

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The Select Committee on Pension Policy

Plan 1 Funding Method

Matt Smith, FCA, MAAA, EA
State Actuary
August 21, 2006

Outline

- Review of policy questions
- Analysis
- Options
- Next steps

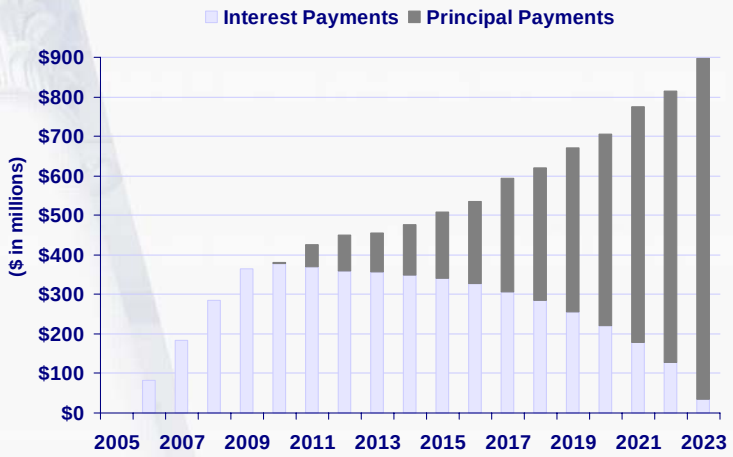
Review of Policy Questions

- Is the Plan 1 funding method serving its intended purpose?
- Will it produce a reasonable and manageable schedule of contributions?
- Is the current method too backloaded?
- Should Plan 1 benefit improvements have a separate funding policy?
- How do you balance the need to fund unfunded prior costs with the need for benefit improvements?

Analysis

- Current method spreads unfunded liability over projected system payroll assumed to grow by:
  - 4.5% annual pay increases; and
  - 1.25% (0.90% in TRS) annual growth in system membership
- Produces a "level percentage of system payroll" payment schedule
- Produces a "back-loaded dollar" payment schedule

PERS 1 UAAL Payment Schedule – Current Method*



•Schedule provided for illustrative purposes only. Does not represent the actual amortization schedule.

Analysis

- Risk factors
  - payroll and membership may grow less than assumed
  - trust fund may return less than 8% assumed rate
  - state and local tax revenues may grow less than assumed payroll and membership growth
- Benefit improvements for past service increase the impact of these risks

Analysis

- If these risks become reality
  - current method may produce an unreasonable schedule of contributions
  - contributions may be deferred or skipped
  - unfunded prior service costs will remain
  - plan costs will increase

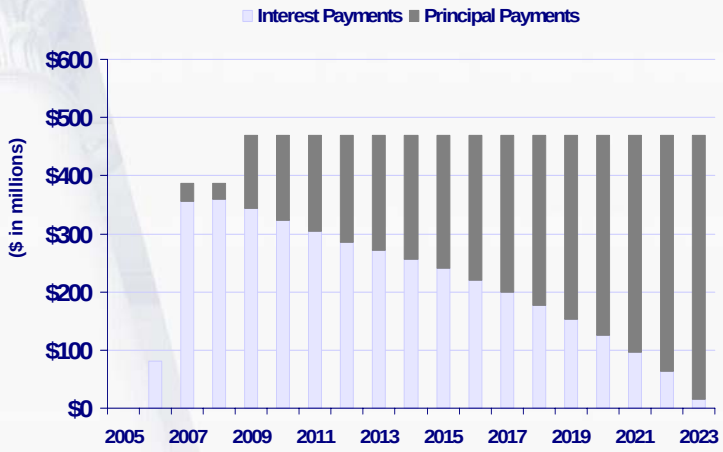
Options

- Method change
- Assumption change
- Identify additional funding sources
- Asset and liability management
- Separate funding policy for benefit improvements
- Combination of options

Method Change

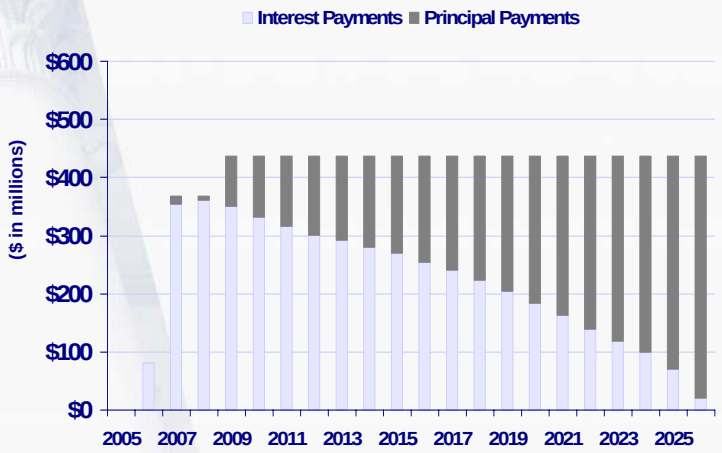
- Switch to level dollar
  - retain current amortization date or extend
- Reduces backloading under current method
- Reduces risk that payments outpace tax revenues

PERS 1 UAAL Payment Schedule – Level Dollar to 2024*



** 17 level payments at 8% annual interest; starting in 2007. Schedule provided for illustrative purposes only.*

PERS 1 UAAL Payment Schedule – Level Dollar to 2027*



** 20 level payments at 8% annual interest; starting in 2007. Schedule provided for illustrative purposes only.*

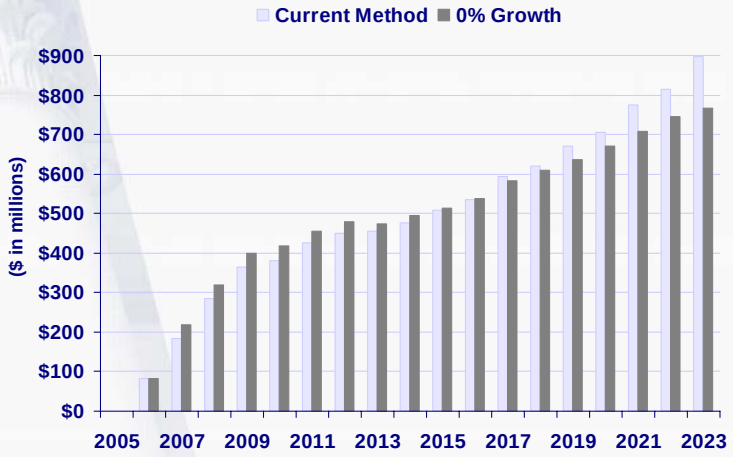
Method Changes

Projected Fiscal Impacts Fiscal Cost Summary				
Cost ($ in Millions)	Level Dollar		Level Dollar to 2027	
	PERS 1	TRS 1	PERS 1	TRS 1
2007-09				
Employer Total	$304.6	$168.4	$265.8	$144.8
General Fund State	63.4	113.7	55.3	97.7
25-year				
Employer Total	(1,733.6)	(1,202.7)	(563.3)	(310.5)
General Fund State	(360.6)	(811.9)	(117.2)	(209.6)

Assumption Change

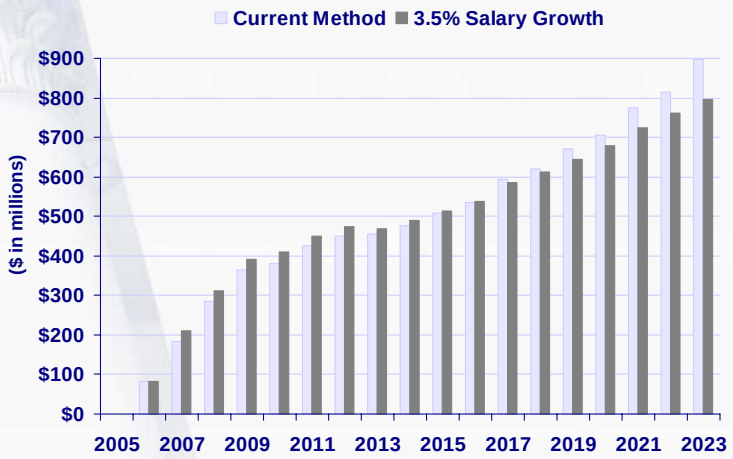
- Retain current method
- Remove membership growth assumption
- Lower salary growth assumption to 3.5%
- Shorten the amortization period to 2019

PERS 1 UAAL Payment Schedule – 0% Membership Growth*



•Schedule provided for illustrative purposes only. Does not represent the actual amortization schedule.

PERS 1 UAAL Payment Schedule – 3.5% Salary Growth*



•*Schedule provided for illustrative purposes only. Does not represent the actual amortization schedule.*

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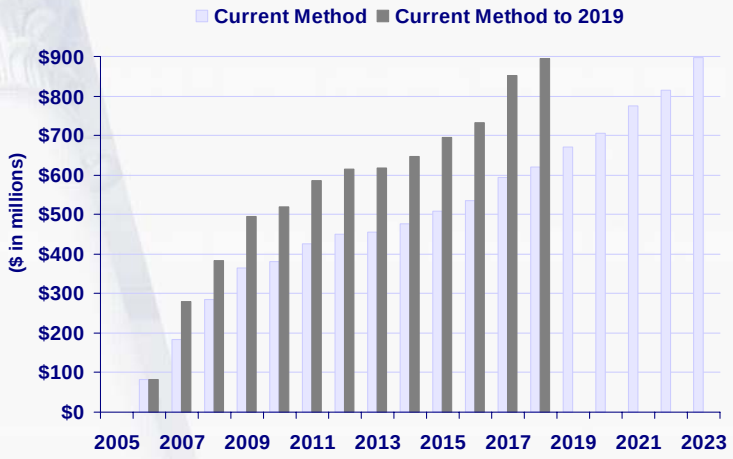
PERS 1 UAAL Payment Schedule – Current Method to 2019*



•*Schedule provided for illustrative purposes only. Does not represent the actual amortization schedule.*

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Assumption Changes

Projected Fiscal Impacts Fiscal Cost Summary						
Cost ($ in Millions)	0% Growth		3.5% Salary		Current to 2019	
	PERS 1	TRS 1	PERS 1	TRS 1	PERS 1	TRS 1
2007-09						
Employer Total	$68.1	$29.5	$52.0	$32.1	$194.2	$119.6
General Fund State	14.2	19.9	10.8	21.7	40.4	80.8
25-year						
Employer Total	(120.3)	(44.6)	(89.0)	(43.0)	(1,748.4)	(1,243.2)
General Fund State	(25.0)	(30.1)	(18.5)	(29.0)	(363.7)	(839.2)

Identify Additional Funding Sources

- Examples of non-payroll related contributions:
  - new tax
    - Insurance premium tax (Oklahoma Police Pension Retirement Plans)
  - new fee
    - Accident report fee (West Virginia Deputy Sherriff's)
  - general fund appropriations (New York, Montana, West Virginia)
  - periodic appropriations for UAAL (Connecticut, Montana, Illinois, Rhode Island)

Identify Additional Funding Sources

- Other considerations:
  - 601 expenditure-cap issues?
  - Constitutional issues?

Asset and Liability Management

- Study separately for PERS 1 and TRS 1
- Set risk tolerance for upward volatility in Plan 1 UAAL contributions
- Select asset allocation policy that achieves
  - lowest upward volatility at the lowest expected cost
- Separate PERS 1 and TRS 1 from the commingled trust fund?

Separate Funding Policy for Benefit Improvements

- Separately amortize future benefit increases over
  - 10 years of projected system payroll; or
  - average expected future lifetime of Plan 1 members
  - whichever is less

Next Steps?

- Next scheduled subgroup meeting
  - September 18, 2006
- Direction to staff