SENATE BILL REPORT
SB 6101

As Reported By Senate Committee On:
Ways & Means, April 4, 2005

Title: An act relating to public pensions.

Brief Description: Modifying public pension provisions.

Sponsors: Senator Prentice.

Brief History:
Committee Activity: Ways & Means: 4/1/05, 4/4/05 [DPS, DNP, w/oRec].

SENATE COMMITTEE ON WAYS & MEANS

Majority Report: That Substitute Senate Bill No. 6101 be substituted therefor, and the substitute bill do pass.
Signed by Senators Prentice, Chair; Doumit, Vice Chair; Fairley, Kohl-Welles, Pridemore, Rasmussen, Regala, Rockefeller and Thibaudeau.

Minority Report: Do not pass.
Signed by Senator Zarelli, Ranking Minority Member.

Minority Report: That it be referred without recommendation.
Signed by Senators Brandland, Parlette, Pflug, Roach and Schoesler.

Staff: Erik Sund (786-7454)

Background: The Office of the State Actuary (OSA) is responsible for recommending appropriate member and employer contribution rates for the Public Employees', Teachers', School Employees', and Washington State Patrol Retirement Systems (PERS, TRS, SERS, and WSPRS) to the Pension Funding Council (PFC), which adopts the rates for each fiscal biennium. Included as part of the rates recommended by the State Actuary to the PFC for the 2005-07 biennium were pre-funding for the gain-sharing benefit in the Plans 1 and 3 and contributions towards paying off the unfunded liabilities in the Plans 1.

Gain-sharing was created by the 1998 Legislature as a mechanism to increase member benefits in PERS 1, PERS 3, TRS 1, TRS 3, and SERS 3. These increases occur whenever there are extraordinary investment gains - which are defined as compound average of investment returns on pension fund assets that exceed 10 percent over a period of four fiscal years. Gain-sharing calculations are currently made once each biennium with potential distributions occurring in January of even-numbered years. In Plan 1, half of all extraordinary gains are used to enhance the Uniform Cost-of-Living Adjustment (Uniform COLA) that is given to eligible retirees each year. The other half of extraordinary returns is used to help pay off the unfunded liability in PERS 1 and TRS 1. In Plan 3, half of the extraordinary gains are paid directly into eligible members' defined contribution accounts. There have been two gain-sharing distributions since 1998 which resulted in combined benefit improvements costing roughly $1.1 billion.

At the present time there is no codified policy for funding the benefits associated with gain-sharing. The cost of future gain-sharing has never been reflected in the basic contribution rates for the affected systems and was not included in the 2002 actuarial valuation, as the funding methodology and materiality of the gain-sharing provisions were under review. The recent 2003 Actuarial Valuation Report (prepared in December 2004) identified gain-sharing as a material liability and reflected in the basic contribution rates recommended by the State Actuary to the PFC.

When the gain-sharing benefit was created by the 1998 Legislature, language was included in the law to reserve the right of the Legislature to amend or repeal the gain-sharing benefits.

While the state retirement plans that are currently open to new members (the Plans 2 and 3) are currently fully funded, unfunded accrued actuarial liabilities (UAALs) exist in both PERS 1 and TRS 1. This means that the value of the plan liabilities, in the form of members' earned benefits to date, are exceeded by the value of the plan assets. As of the most recent actuarial valuation, the UAAL for PERS 1 is $2.6 billion and the UAAL for TRS 1 is $1.4 billion. The statutory funding policy for paying off the UAAL in the Plans 1 is codified as a goal within the actuarial funding chapter. RCW 41.45.010(2) states that the funding process for the state retirement systems is intended to fully amortize the total Plan 1 costs by not later than June 30, 2024. The payments towards the Plan 1 UAAL are included in employer rates and are not shared by members. Under Chapter 11 of the Laws of 2003 (EHB 2254) the Legislature suspended the employer contributions towards the PERS 1 and TRS 1 unfunded liabilities for the duration of the 2003-05 biennium.

The State Actuary's recommended employer 2005-07 contribution rates under current law are 5.73 percent for PERS, 6.74 percent for TRS, and 7.56 percent for SERS. The recommended Plan 2 member rates for the same period are 3.38 percent for PERS 2, 2.48 percent for TRS 2, and 3.51 percent for SERS 2. Member rates in PERS 1 and TRS 1 are fixed at 6 percent. Member contributions in PERS 3, TRS 3, and SERS 3 are made into members' individual defined contribution accounts and do not affect pension system funding.

Summary of Substitute Bill: Gain-sharing benefit distributions are made at the discretion of the Legislature rather than occurring automatically. The cost of gain-sharing is not to be incorporated in the basic contribution rates until after a distribution has been made. Payments towards the unfunded liabilities in PERS 1 and TRS 1 are suspended for the 2005-07 biennium. Pension contribution rates are adjusted accordingly. As a result of these policy changes, new employer contribution rates are adopted for 2005-07. The employer rates are 3.38 percent for PERS, 2.74 percent for TRS, and 3.51 percent for SERS. Member contribution rates are unaffected.

Substitute Bill Compared to Original Bill: The substitute bill contains a number of technical corrections, including the removal of references to rates for the Law Enforcement Officers' and Fire Fighters' Retirement System Plan 2 (LEOFF 2), which is not affected by the bill.

Appropriation: None.

Fiscal Note: Available.

Committee/Commission/Task Force Created: No.

Effective Date: The bill contains multiple effective dates. Please refer to the bill.

Testimony For: None.

Testimony Against: This bill may save the state some money but it will hurt current and future retirees in the Plans 1 and 3. Many members that moved to Plan 3 were counting on the gain-sharing benefit when they made their decision and were not aware that the Legislature reserve the right to amend or repeal the benefit. The proposal to replace gain-sharing with an alternative package of more certain but less expensive benefits, which was recommended by the Select Committee on Pension Policy, is preferable to this bill.

Who Testified: CON: Cassandra de la Rosa, Retired Public Employees Council; Ed Gonion, Washington State School Retirees' Association; John Kvamme, Washington Association of School Administrators & Association of Washington School Principals; Leslie Main, Washington State School Retirees' Association; Randy Parr, Washington Education Association; Pat Thompson, Washington State Council of County & City Employees; David Westberg, AFL-CIO Stationary Engineers.