

# Smoothing Corridor

1 AN ACT Relating to establishing an asset smoothing corridor for  
2 actuarial valuations used in the funding of the state retirement  
3 systems; and amending RCW 41.45.020 and 41.45.035.

4 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

5 **Sec. 1.** RCW 41.45.020 and 2003 c 295 s 8 are each amended to read  
6 as follows:

7 As used in this chapter, the following terms have the meanings  
8 indicated unless the context clearly requires otherwise.

9 (1) "Council" means the pension funding council created in RCW  
10 41.45.100.

11 (2) "Department" means the department of retirement systems.

12 (3) "Law enforcement officers' and fire fighters' retirement system  
13 plan 1" and "law enforcement officers' and fire fighters' retirement  
14 system plan 2" means the benefits and funding provisions under chapter  
15 41.26 RCW.

16 (4) "Public employees' retirement system plan 1," "public  
17 employees' retirement system plan 2," and "public employees' retirement  
18 system plan 3" mean the benefits and funding provisions under chapter  
19 41.40 RCW.

1 (5) "Teachers' retirement system plan 1," "teachers' retirement  
2 system plan 2," and "teachers' retirement system plan 3" mean the  
3 benefits and funding provisions under chapter 41.32 RCW.

4 (6) "School employees' retirement system plan 2" and "school  
5 employees' retirement system plan 3" mean the benefits and funding  
6 provisions under chapter 41.35 RCW.

7 (7) "Washington state patrol retirement system" means the  
8 retirement benefits provided under chapter 43.43 RCW.

9 (8) "Unfunded liability" means the unfunded actuarial accrued  
10 liability of a retirement system.

11 (9) "Actuary" or "state actuary" means the state actuary employed  
12 under chapter 44.44 RCW.

13 (10) "State retirement systems" means the retirement systems listed  
14 in RCW 41.50.030.

15 (11) "Classified employee" means a member of the Washington school  
16 employees' retirement system plan 2 or plan 3 as defined in RCW  
17 41.35.010.

18 (12) "Teacher" means a member of the teachers' retirement system as  
19 defined in RCW 41.32.010(15).

20 (13) "Select committee" means the select committee on pension  
21 policy created in RCW 41.04.276.

22 (14) "Actuarial value of assets" means the value of pension plan  
23 investments and other property used by the actuary for the purpose of  
24 an actuarial valuation.

25 **Sec. 2.** RCW 41.45.035 and 2003 1st sp.s. c 11 s 1 are each amended  
26 to read as follows:

27 (1) Beginning July 1, 2001, the following long-term economic  
28 assumptions shall be used by the state actuary for the purposes of RCW  
29 41.45.030:

30 (a) The growth in inflation assumption shall be 3.5 percent;

31 (b) The growth in salaries assumption, exclusive of merit or  
32 longevity increases, shall be 4.5 percent;

33 (c) The investment rate of return assumption shall be 8 percent;  
34 and

35 (d) The growth in system membership assumption shall be 1.25  
36 percent for the public employees' retirement system, the school

1 employees' retirement system, and the law enforcement officers' and  
2 fire fighters' retirement system. The assumption shall be .90 percent  
3 for the teachers' retirement system.

4 (2)(a) Beginning with actuarial studies done after July 1, 2003,  
5 changes to plan asset values that vary from the long-term investment  
6 rate of return assumption shall be recognized in the actuarial value of  
7 assets over a period that varies up to eight years depending on the  
8 magnitude of the deviation of each year's investment rate of return  
9 relative to the long-term rate of return assumption. Beginning with  
10 actuarial studies performed after July 1, 2004, the actuarial value of  
11 assets shall not be greater than one hundred thirty percent of the  
12 market value of assets as of the valuation date or less than seventy  
13 percent of the market value of assets as of the valuation date.  
14 Beginning April 1, 2004, the council, by affirmative vote of four  
15 councilmembers, may adopt changes to this asset value smoothing  
16 technique. Any changes adopted by the council shall be subject to  
17 revision by the legislature.

18 (b) The state actuary shall periodically review the appropriateness  
19 of the asset smoothing method in this section and recommend changes to  
20 the legislature as necessary.

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# FISCAL NOTE – DRAFT

REQUEST NO.

RESPONDING AGENCY:	CODE:	DATE:	BILL NUMBER:
Office of the State Actuary	035	12/09/03	Z-0872.1/04

## SUMMARY OF BILL:

This bill impacts the Public Employees, School Employees, Teachers, Law Enforcement and Fire Fighters and State Patrol Retirement Systems by limiting the amount that the actuarial or “smoothed” value of assets may deviate from the underlying market value of assets for purposes of determining employer contributions in Plans 1 and 2/3 and employee contributions in the Plans 2.

Beginning with actuarial studies performed after July 1, 2004, the actuarial value of assets would not be allowed to exceed 130% of the market value of assets or drop below 70% of the market value of assets as of the valuation date.

This bill would require the state actuary to periodically review the appropriateness of the asset smoothing method and recommend changes to the legislature as necessary.

Effective Date: 90 days after session.

## CURRENT SITUATION:

The current asset smoothing method defined under RCW 41.45.035 has no restrictions on the amount that the “smoothed” or actuarial value of assets may deviate from the underlying market value of assets.

## MEMBERS IMPACTED:

This bill would affect future employee contribution rates in PERS 2, SERS 2, TRS 2, LEOFF 2 and in WSPRS when the 30% market value corridor is triggered in the future. In total, there were 162,664 active members in PERS 2, SERS 2, TRS 2, LEOFF 2 and in WSPRS as of September 30, 2002.

## FISCAL IMPACT:

Estimated long-term fiscal impact: None

As of the latest actuarial valuation report (9/30/2002), the ratio of the actuarial value of assets to the market value of assets was 130% (for all systems combined). This ratio varies by system and plan (see table below).

**Ratio of Actuarial to Market Value of Assets as of 9/30/2002**

PERS 1	PERS 2/3	TRS 1	TRS 2/3	SERS 2/3	LEOFF 1	LEOFF 2	WSP
131%	130%	135%	132%	131%	125%	124%	125%

**Ratio of Actuarial to Market Value of Assets as of 9/30/2003\***

PERS 1	PERS 2/3	TRS 1	TRS 2/3	SERS 2/3	LEOFF 1	LEOFF 2	WSP
118%	116%	124%	120%	116%	110%	109%	110%

\* Estimate

The proposed smoothing corridor would begin with actuarial studies performed after July 1, 2004 and as a result would first apply to the September 30, 2003 actuarial valuation. There would be no long-term impact on projected contribution rates, based on an investment return assumption of 8% per year, since the actuarial value of assets for each system and plan is within the 30% corridor as of September 30, 2003.

Actual investment experience over short-term periods will vary. Successive years of significant investment gains or losses, relative to the 8% assumption, over a short-term experience period may cause the actuarial value of assets to fall outside the proposed smoothing corridor. Under these circumstances, the proposed smoothing corridor would decrease contribution rates when plan asset values fall below the corridor and increase contribution rates when asset values exceed the corridor.