LEOFF Plan 2 Funding Policy Work Session

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Office of the State Actuary
"Securing tomorrow's pensions today."

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Today's Presentation

- Background on current funding policy
- Results of actuarial valuation and audit
- Expected future contribution rates and funded status
- Possible funding policy options for discussion
- No Board action required today

Current Board Funding Policy

- Aggregate cost method used to determine contribution requirements
- L2 Board adopted additional rate stability measures
  - 2004: 90 percent of the normal cost under the Entry Age Normal (EAN) cost method, effective July 1, 2009
  - 2008: 100 percent of the normal cost under EAN for 2009-2013
  - 2010: Maintain current rates through 2011-2017
- Funded status calculated under Projected Unit Credit (PUC)
  - Aggregate cost method does not provide a useful funded status measure
  - GASB now requires use of EAN for financial reporting
  - Actuarial valuations will report funded status using EAN starting June 30, 2014
- Additional information provided at September 2013 Board meeting

Actuarial Valuation Results – 2015-2017 Contribution Rates

Employee and Employer/State Contribution Rates				
	Aggregate	90% EANC	100% EANC	Adopted
Employee	6.98%	7.97%	8.85%	8.41%
Employer*	4.19%	4.78%	5.31%	5.05%
State	2.79%	3.19%	3.54%	3.36%

Based on the June 30, 2013 Actuarial Valuation Report.

**Excludes current administrative expense rate of 0.18%.*

Actuarial Valuation Results – Funded Status

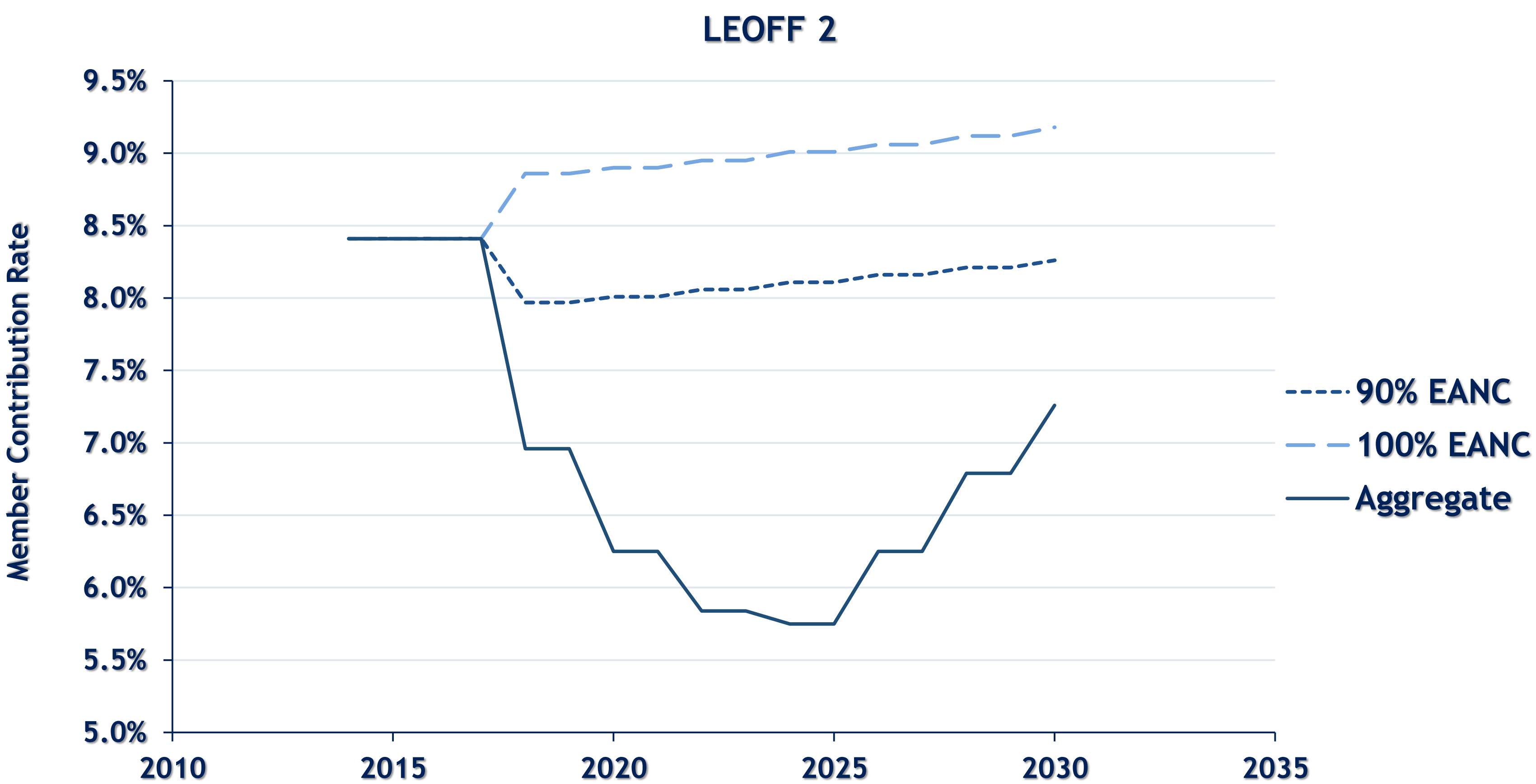
Funded Status At June 30, 2013	
(Dollars in Millions)	
a. Present Value of "Earned" Benefits	$6,859
b. Market Value of Assets	7,637
c. Deferred Gains/(Losses)	(225)
d. Actuarial Value of Assets (b-c)	7,862
e. Unfunded Liability (a-d)	($1,003)
f. Funded Ratio (d/a)	115%

Note: Totals may not agree due to rounding.

Outside Audit Found No Material Differences

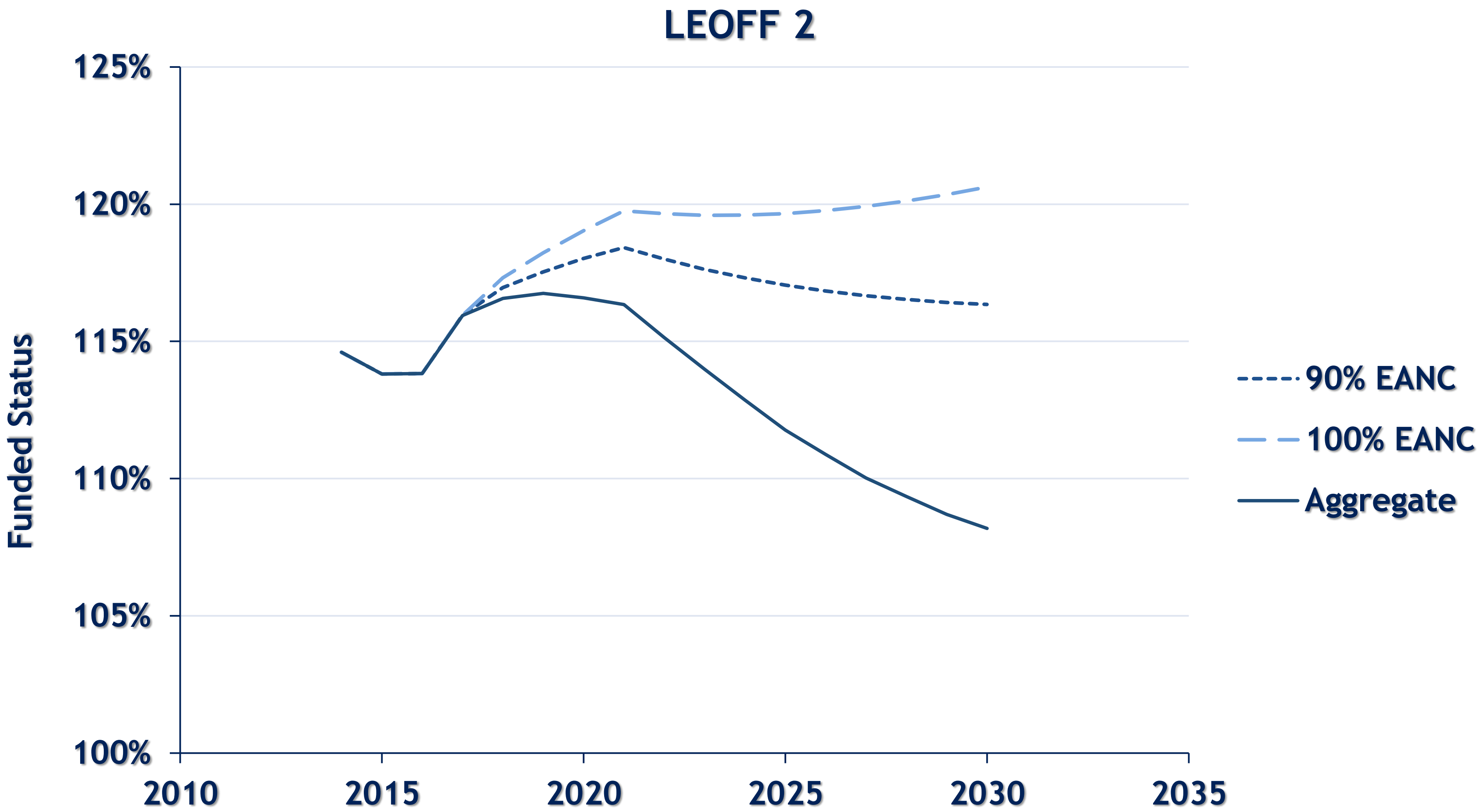
- Commented on current funding policy
  - Doesn't address stable rate policy if funded status continues to increase
  - Board may want to proactively consider action plan
- Auditor provided suggestions the Board could consider
  - De-risk retiree liabilities
  - Adopt more conservative assumptions
  - Apply funding ratio corridor

Projection Of Expected Member Contribution Rates*



**Based on the June 30, 2013 Actuarial Valuation Report, actual assets through June 30, 2014, projection assumptions as disclosed on the OSA website, and all assumptions are realized.*

Projection Of Expected Funded Status Ratios*



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Current Funding Policy Provides Stability And Higher Funded Status

- Member rates under EANC increase gradually
  - Fifty basis points over ten-year period
- Member rates under Aggregate have more volatility
  - Decrease about 120 basis points over a six-year period
  - Increase about 50 basis points each biennium after
- Expected funded status increases above 120 percent under 100 percent EANC

Funding Policy Considerations

- Funding policy determines contribution rates
  - Adequacy, stability, affordability
- Complexity of the policy can impact understandability and administration
- Continue with current policy
  - Aggregate cost method with EANC rate floor for stability
  - Regularly monitor funded status progress including future expectations
- Adopt new funding policy
  - Change underlying actuarial cost method
  - Adopt new rate stability measure(s)
  - Consider options and pros/cons

Possible New Funding Policy Options

- Change underlying actuarial cost method to EAN
  - Currently using normal cost from EAN
  - EAN includes Unfunded Actuarial Accrued Liability (UAAL) component
    - UAAL can be positive or negative
    - Requires amortization policy
- Change rate stability measure when funded status hits certain targets
  - Example: 100 percent EANC when funded status is below 120 percent and 80 percent EANC when funded status is 120 percent or higher
- Set policy and adopt rates within that policy
  - Target contribution rate
  - Target changes if funded status hits specified corridor
  - Example: 18 percent total rate when funded status between 80 percent and 120 percent (20 percent corridor)

Possible Pros And Cons For Policy Options

Funding Policy Options	Pros	Cons
Rate stability measure based on funded status targets	Gradual change, keeps Aggregate as base method, lines up with current practice, not dramatic policy change.	Complicated, rates could vary more (not as stable).
EAN actuarial cost method	Simple, most common method used by public plans, 'GASB approved'.	UAAL requires amortization policy, UAAL impacts intergenerational equity, not base method used by other WA State plans.
Target rate within funded status corridor	Rate stability, known rates when funded status within corridor.	Not clear actuarial methodology, policy needed when funded status hits corridor.

Response To Audit Comments

- De-risk retiree liabilities
  - Viable option
  - Consider as separate study outside funding policy
  - Determine retiree liability risk and how to manage it
- Adopt more conservative assumptions
  - "More conservative" interpreted as not best estimate
  - Would reduce funded status measure
  - Could lead to higher required contributions
  - Could affect goal of intergenerational equity
- Apply funding ratio corridor
  - Included as possible new funding policy option

Funding Policy Important To Success Of Pension Program

- Balance affordability and risk
- Stable rates lead to stable pension budgets
- Complicated policies can be misunderstood
- Consider funding goals in statute
  - Fully fund the plan as provided by law
  - Establish long-term employer rates that remain relatively predictable proportion of future state budgets
  - Intergenerational equity

Questions?