

# BOARD MEETING AGENDA

SEPTEMBER 29, 2021 • 9:30AM



## LOCATION

Zoom Video Conference

## TRUSTEES

DENNIS LAWSON, CHAIR  
Central Pierce Fire and Rescue

JASON GRANNEMAN, VICE CHAIR  
Clark County Sheriff's Office

ADE' ARIWOOLA  
City of Federal Way

MARK JOHNSTON  
Vancouver Fire Department

AJ JOHNSON  
Snohomish County Fire

SENATOR JEFF HOLY  
Spokane Police Department (Ret)

TARINA ROSE-WATSON  
Spokane Int'l Airport Police Dept

PAT MCELLIGOTT  
City of Dupont

REPRESENTATIVE STEVE BERGQUIST  
WA State Representative

WOLF OPITZ  
Pierce County

SENATOR ANN RIVERS  
WA State Senator

## STAFF

Steve Nelsen, Executive Director  
Tim Valencia, Deputy Director  
Jessie Jackson, Executive Assistant  
Jessica Burkhart, Administrative Services Manager  
Jacob White, Senior Research and Policy Manager  
Karen Durant, Senior Research and Policy Manager  
Tammy Sadler, Benefits Ombudsman  
Tor Jernudd, Assistant Attorney General

**THEY KEEP US SAFE,  
WE KEEP THEM SECURE.**

- |  |                 |
|--|-----------------|
| <b>1. Approval of Minutes</b>  | <b>9:30 AM</b>  |
| <b>2. DRS Benchmarking</b><br>Mark Feldhausen, Budget Director   | <b>9:35 AM</b>  |
| <b>3. Report on Financial Condition (OSA)</b><br>Matt Smith, State Actuary                                 | <b>10:05 AM</b> |
| <b>4. Recommendation on Long-Term Economic Assumptions (OSA)</b><br>Mitch DeCamp, Senior Actuarial Analyst | <b>10:30 AM</b> |
| <b>5. AGO Board Training</b><br>Tor Jernudd, Asst Attorney General, AGO                                    | <b>11:00 AM</b> |
| <b>6. Board Officer Elections</b>  | <b>11:45 AM</b> |
| <b>7. Administrative Update</b> <ul style="list-style-type: none"><li>• Outreach Activities</li></ul>      | <b>12:00 PM</b> |
| <b>8. Interruptive Military Service Credit Follow-up</b><br>Jacob White, Sr Research and Policy Manager    | <b>12:15 PM</b> |
| <b>9. Benefit Improvement Account Educational Follow-up</b><br>Jacob White, Sr Research and Policy Manager | <b>12:45 PM</b> |
| <b>10. Survivor Option Reelection Follow-up</b><br>Jacob White, Sr Research and Policy Manager             | <b>1:15 PM</b>  |

*\*Lunch is served as an integral part of the meeting.*

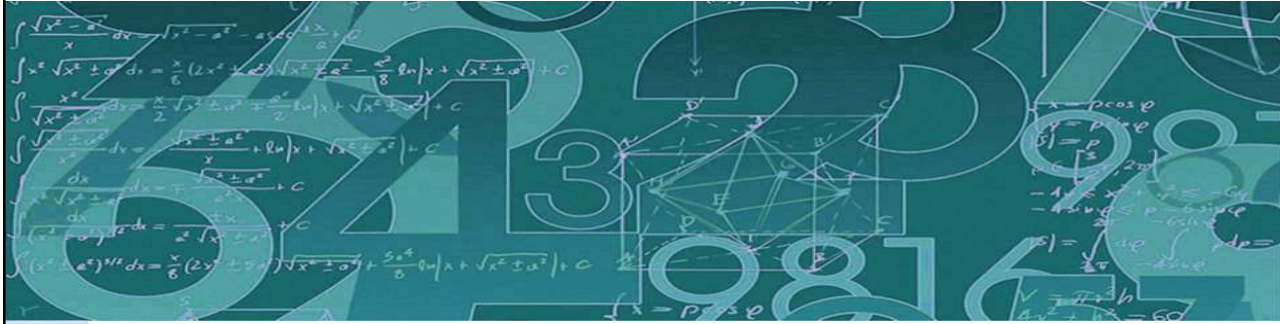
*In accordance with RCW 42.30.110, the Board may call an Executive Session for the purpose of deliberating such matters as provided by law. Final actions contemplated by the Board in Executive Session will be taken in open session. The Board may elect to take action on any item appearing on this agenda.*

## Report on Financial Condition

$$\int x^2 \sqrt{x^2 \pm a^2} dx = \frac{x}{6} (2x^2 \pm a^2) \sqrt{x^2 \pm a^2} - \frac{a^2}{8} \ln|x + \sqrt{x^2 \pm a^2}| + C$$

Presentation to: LEOFF 2 Retirement Board

Mitch DeCamp, Senior Actuarial Analyst



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"Supporting financial security for generations."

September 29, 2021

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## Today's Presentation

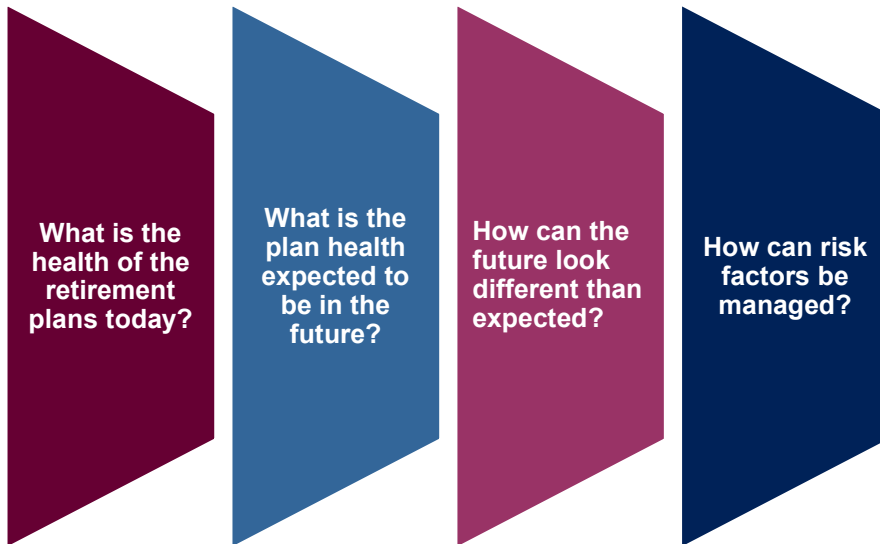
- Highlights of the *Report on Financial Condition*
  - Published jointly with the *Economic Experience Study*
- Link to the full reports included in the Appendix
- Impacts of FY 2021 investment return
- No action required at today's meeting

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## Framework for Assessing Financial Condition



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## Measures for Assessing Plan Health

- **Affordability: Ability to provide adequate funding**
  - Can members, employers, and the state pay the amount required to fully fund the plans?
  - Examples: Contribution rate levels, pension contributions relative to state budget
- **Solvency: Ability to pay for member benefits**
  - Can the plans pay the benefits that have been earned by members?
  - Are the plans on target to meet future benefit requirements?
  - Example: Funded ratio



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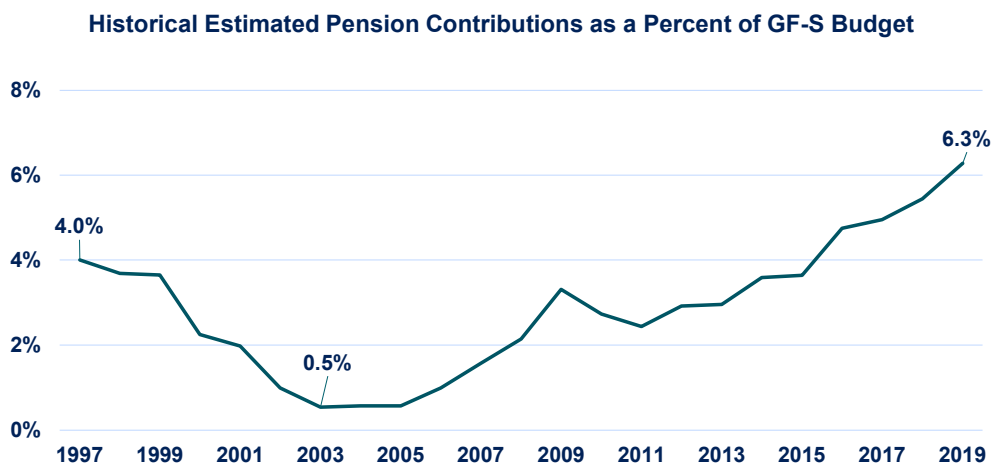
## Current Contribution Rates Declining after Historically High Levels

- Phase-in complete of increased costs due mortality assumption change
- Recent investment returns higher than assumed
- Plan 1 UAAL contribution rates have declined to minimum levels
- For most plans, cost of new hires is less than current members

| Total Employer Contribution Rates |                    |                    |                    |                  |
|-----------------------------------|--------------------|--------------------|--------------------|------------------|
|                                   | 2015-17            | 2017-19            | 2019-21            | 2021-23          |
| System                            | Biennium Collected | Biennium Collected | Biennium Collected | Biennium Adopted |
| PERS                              | 11.00%             | 12.52%             | 12.68%             | 10.07%           |
| TRS                               | 12.95%             | 15.02%             | 15.33%             | 14.24%           |
| SERS                              | 11.40%             | 13.30%             | 13.01%             | 11.47%           |
| PSERS                             | 11.36%             | 11.76%             | 11.96%             | 10.21%           |
| LEOFF                             | 8.41%              | 8.75%              | 8.59%              | 8.53%            |
| WSPRS                             | 8.01%              | 12.81%             | 17.50%             | 17.66%           |

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## Pension Contributions Are Larger Portion of State Budget



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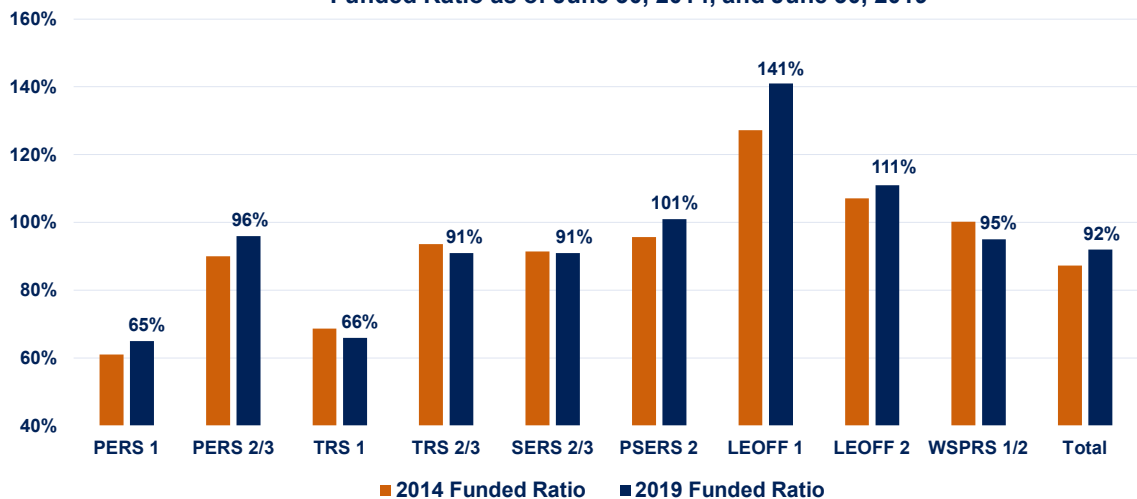
## We Rely on Funded Ratio to Measure Solvency

- Funded ratio compares plan assets to members' earned benefits
- Plan assets reflect past funding plus investment earnings
- Funded ratio >100% means the plan has more assets than earned benefits

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## Funded Ratio Generally Increased from 2014

Funded Ratio as of June 30, 2014, and June 30, 2019



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## Plan Financial Health: What Does the Future Hold?

- Continued improvement for future affordability and solvency metrics
  - Assumes actual experience matches assumptions over long term
  - Excludes impact from FY 2021 investment return
- Contribution rates expected to decline
  - Contributions as a percent of General-Fund Budget expected to decline from a high of 6.4% in 2020 to 3.3% in 2028
- All plans on target to reach full funding
  - All open plans projected to have a funded ratio of 95% or higher by 2023
  - PERS 1 and TRS 1 UAAL projected to be paid off in 2027 and 2026, respectively

## The Future Might Be Different than We Expect

- OSA's risk assessment model simulates 2,000 different investment return scenarios
- Assess risks under Current Law and "Past Practices"
- Please refer to the RFC for likelihood of various projected affordability and solvency measures
  - Select Measures of Pension Risk table
- Affordability and solvency risk measures have improved
- [Commentary on Risk](#) webpage provides additional risk analysis and sensitivity of financial measures

## 2021 Was Different than Expected

- June 2021 revenue forecast better outlook than June 2020 revenue forecast
- Investment return on pension assets for FYE June 30, 2021, almost 29%
  - Highest single year return in over 30 years
  - Approximately \$22 billion in investment earnings above assumed
  - Will any be given back through a market downturn?



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## AVA Accounts for Unexpected Investment Returns

- Develop Actuarial Value of Assets (AVA) by smoothing past and current asset gains (or losses) from investments
  - Calculate asset gain (or loss) based on 7.4% expected return
  - Smooth gain (or loss) over a period up to 8 years
  - Smoothing method reduces contribution rate and funded status volatility

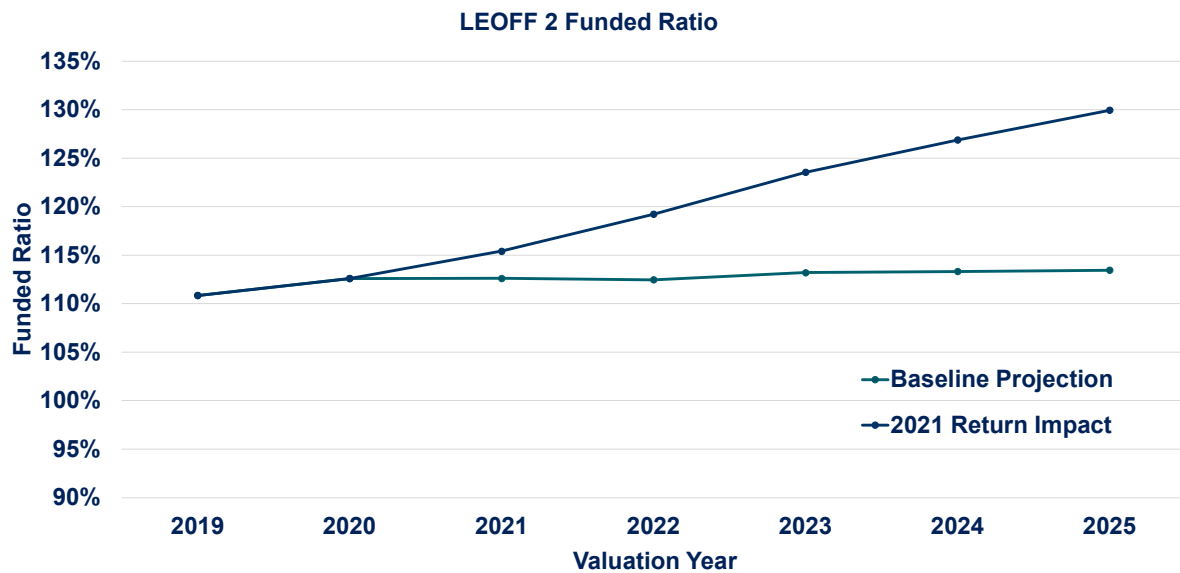
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## Smoothing Annual Investment Returns

| Smoothing Schedule     |                  |                    |
|------------------------|------------------|--------------------|
| LEOFF 2 Rate of Return | Smoothing Period | Annual Recognition |
| 14.4% and up           | 8 years          | 12.50%             |
| 13.4%-14.4%            | 7 years          | 14.29%             |
| 12.4%-13.4%            | 6 years          | 16.67%             |
| 11.4%-12.4%            | 5 years          | 20.00%             |
| 10.4%-11.4%            | 4 years          | 25.00%             |
| 9.4%-10.4%             | 3 years          | 33.33%             |
| 8.4%-9.4%              | 2 years          | 50.00%             |
| 6.4%-8.4%              | 1 year           | 100.00%            |
| 5.4%-6.4%              | 2 years          | 50.00%             |
| 4.4%-5.4%              | 3 years          | 33.33%             |
| 3.4%-4.4%              | 4 years          | 25.00%             |
| 2.4%-3.4%              | 5 years          | 20.00%             |
| 1.4%-2.4%              | 6 years          | 16.67%             |
| 0.4%-1.4%              | 7 years          | 14.29%             |
| 0.4% and lower         | 8 years          | 12.50%             |

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## 2021 Asset Gains Increases LEOFF 2 Funded Ratio



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## Reflecting Investment Experience Improves Projected Financial Outcomes

- All open plans projected to have a funded ratio of 100% or higher by 2023
- PERS 1 UAAL projected to be paid off in 2025
- TRS 1 UAAL projected to be paid off in 2024
  - Projected payoff is 2023 if the \$800 million lump sum payment is included
- These projections do not reflect updated EES recommendations

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## Projected Contribution Rates Reflecting FY 2021 Investment Return—Preliminary

| Total Employer Contribution Rates |                     |                     |                     |                     |
|-----------------------------------|---------------------|---------------------|---------------------|---------------------|
|                                   | 2021-23<br>Biennium | 2023-25<br>Biennium | 2025-27<br>Biennium | 2027-29<br>Biennium |
| System                            | <i>Adopted</i>      | <i>Projected</i>    | <i>Projected</i>    | <i>Projected</i>    |
| <b>PERS</b>                       | 10.07%              | 8.55%               | 4.38%               | 4.38%               |
| <b>TRS</b>                        | 14.24%              | 13.40%              | 5.77%               | 5.24%               |
| <b>SERS</b>                       | 11.47%              | 10.12%              | 4.72%               | 4.72%               |
| <b>PSERS</b>                      | 10.21%              | 9.76%               | 5.46%               | 5.28%               |
| <b>LEOFF</b>                      | 8.53%               | 8.53%*              | 7.74%               | 7.78%               |
| <b>WSPRS</b>                      | 17.66%              | 17.65%              | 7.03%               | 6.88%               |

\*Adopted by the LEOFF 2 Board.

- PERS 1 and TRS 1 contributions projected to end after 2023-25 Biennium
- Projected rates do not reflect updated EES recommendations

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## Projected Contribution Rates Reflecting FY 2021 Investment Return—Preliminary

| Total Employer Contribution Rates |          |           |           |           |
|-----------------------------------|----------|-----------|-----------|-----------|
|                                   | 2021-23  | 2023-25   | 2025-27   | 2027-29   |
| System                            | Biennium | Biennium  | Biennium  | Biennium  |
|                                   | Adopted  | Projected | Projected | Projected |
| PERS                              | 10.07%   | 8.55%     | 4.38%     | 4.38%     |
| TRS                               | 14.24%   | 13.40%    | 5.77%     | 5.24%     |
| SERS                              | 11.47%   | 10.12%    | 4.72%     | 4.72%     |
| PSERS                             | 10.21%   | 9.76%     | 5.46%     | 5.28%     |
| LEOFF                             | 8.53%    | 8.53%*    | 7.74%     | 7.78%     |
| WSPRS                             | 17.66%   | 17.65%    | 7.03%     | 6.88%     |

\*Adopted by the LEOFF 2 Board.

- PERS 1 and TRS 1 contributions projected to end after 2023-25 Biennium
- Projected rates do not reflect updated EES recommendations

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## LEOFF 2 Funding Policy Impacts—Preliminary

| Change in Total Employer Projected Contribution Rates—Preliminary |              |              |              |
|---|--------------|--------------|--------------|
|   | 2021-23      | 2023-25      | 2025-27      |
|   | Biennium     | Biennium     | Biennium     |
| <b>Baseline Projection</b>  | <b>8.53%</b> | <b>8.53%</b> | <b>7.74%</b> |
| Aggregate   |              | 5.17%        | 4.83%        |
| Minimum Rate*   |              | 7.71%        | 7.74%        |
| <b>2021 Return Impact</b>   | <b>8.53%</b> | <b>8.53%</b> | <b>7.74%</b> |
| Aggregate   |              | 4.42%        | 1.90%        |
| Minimum Rate*   |              | 7.71%        | 7.74%        |

Note: Rates through 2023-25 adopted by the Board and assumed to remain unchanged.

\*Represents a minimum contribution rate at 90% of the Entry Age Normal Cost (EANC) rate based on plan funding policy.

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## Funding Policy Changes Added Protections in Mid 2000s

- 131% funded ratio across all plans in 2000, declined to 99% in 2005
  - Funding shortfall, market downturn, and increased benefits
- New funding policies implemented
  - Asset smoothing period increased to a maximum of 8 years (2003)
  - Minimum employer and employee contribution rates (2006)
    - SCPP sponsored legislation

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## Managing Risks We Can Control



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## Report on Financial Condition: Concluding Comments

- Improved affordability and solvency metrics
  - Contribution rates are beginning to decline after some of the highest in plan history
  - Funded ratios improving
- FY 2021 investment return improves projected financial outcomes
- Managing pension risks requires
  - Regular monitoring
  - Making necessary adjustments
  - Applying discipline and a long-term view when considering benefit changes and contribution requirements

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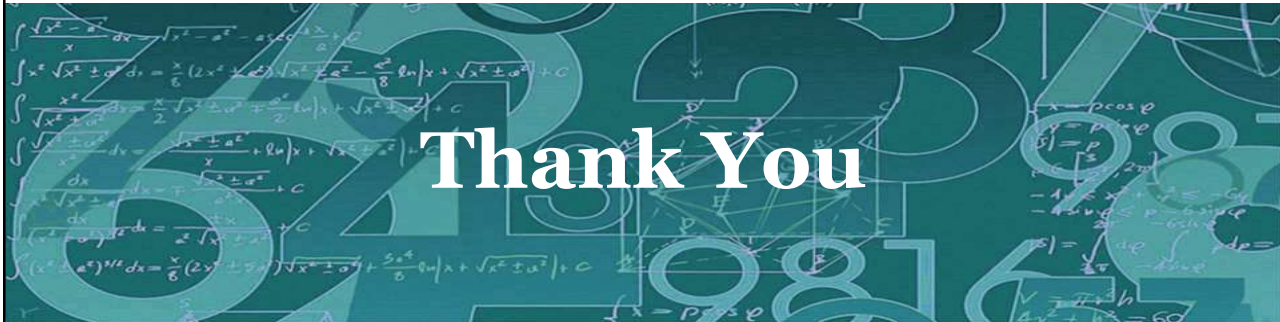
## Questions?



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**Questions? Please Contact: The Office of the State Actuary**  
**[leg.wa.gov/OSA](http://leg.wa.gov/OSA); [state.actuary@leg.wa.gov](mailto:state.actuary@leg.wa.gov)**  
**360-786-6140, PO Box 40914, Olympia, WA 98504**  
**Mitch DeCamp, Senior Actuarial Analyst**

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# Thank You



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## Appendix

- 2021-23 Contribution Rates
- Projected Employee Contribution Rates
- Projection Assumptions and Disclosures
- Please see the full [2021 Report on Financial Condition](#) for more information



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## 2021-23 Contribution Rates

| Adopted 2021-23 Contribution Rates |             |             |       |        |
|------------------------------------|-------------|-------------|-------|--------|
| System                             | Employee    | Employer    |       |        |
|                                    | Normal Cost | Normal Cost | UAAL  | Total  |
| PERS                               | 6.36%       | 6.36%       | 3.71% | 10.07% |
| TRS                                | 8.05%       | 8.05%       | 6.19% | 14.24% |
| SERS                               | 7.76%       | 7.76%       | 3.71% | 11.47% |
| PSERS                              | 6.50%       | 6.50%       | 3.71% | 10.21% |
| LEOFF                              | 8.53%       | 8.53%       | 0.00% | 8.53%  |
| WSPRS                              | 8.61%       | 17.66%      | N/A   | 17.66% |

## Projected Employee Contribution Rates

| Employee Contribution Rates |                            |                              |                              |                              |
|-----------------------------|----------------------------|------------------------------|------------------------------|------------------------------|
| System                      | 2021-23                    | 2023-25                      | 2025-27                      | 2027-29                      |
|                             | Biennium<br><i>Adopted</i> | Biennium<br><i>Projected</i> | Biennium<br><i>Projected</i> | Biennium<br><i>Projected</i> |
| PERS <sup>1</sup>           | 6.36%                      | 4.84%                        | 4.38%                        | 4.38%                        |
| TRS                         | 8.05%                      | 7.21%                        | 5.77%                        | 5.24%                        |
| SERS                        | 7.76%                      | 6.41%                        | 4.72%                        | 4.72%                        |
| PSERS                       | 6.50%                      | 6.05%                        | 5.46%                        | 5.28%                        |
| LEOFF                       | 8.53%                      | 8.53%                        | 7.74%                        | 7.78%                        |
| WSPRS <sup>2</sup>          | 8.61%                      | 8.61%                        | 7.03%                        | 6.88%                        |

*Note: Members in Plan 3 do not make contributions to their defined benefit.*

<sup>1</sup>Plan 1 members' contribution rate is statutorily set at 6.0%.

<sup>2</sup>Current WSPRS member contribution rates are at the maximum for the plan.

- Projected rates include FY 2021 investment return
- Does not reflect updated EES recommendations

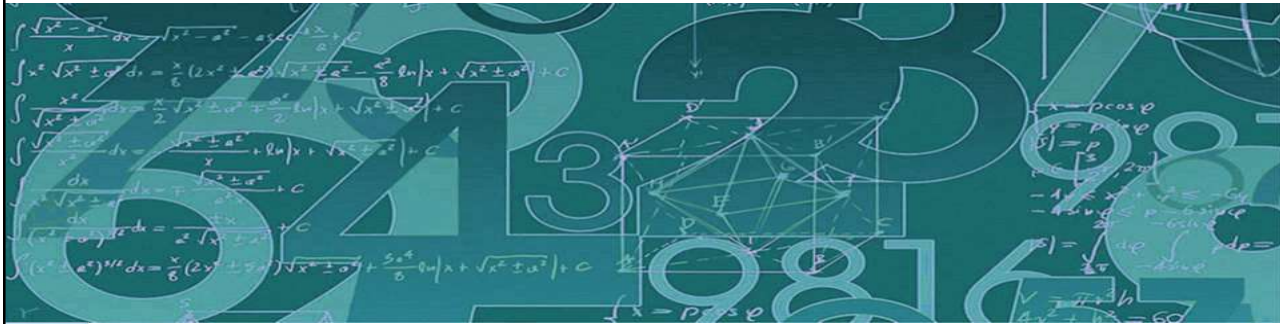
## Projection Assumptions and Disclosures

- The future contribution and rate impacts presented here are preliminary and will change with updates to the underlying data, assumptions, and method
- Analysis based on our [2019 Actuarial Valuation Report](#) and [Projection Assumptions](#)
- We relied on the total CTF time-weighted investment return for FY 2021 of 28.68%
  - Results will change when dollar-weighted system-specific returns are used in the 2021 AVR
- Assumed all future returns beyond 2021 matched the current long-term assumption of 7.5% (7.4% in LEOFF 2)

## State Actuary's Recommendation on Long-Term Economic Assumptions

Presentation to: LEOFF 2 Retirement Board

Matthew M. Smith, State Actuary, FCA, EA, MAAA



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### Today's Presentation

- Highlights of the *Economic Experience Study*
- Full report available on OSA's [website](#)
- Published jointly with the *Report on Financial Condition*

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## A Review of Roles

- Per [RCW 41.45.030\(1\)](#), in odd numbered years, the state actuary makes recommendations on the long-term economic assumptions
- LEOFF 2 Board can adopt changes at any time
- Today's presentation is intended to assist you in determining whether to adopt changes to the plan's economic assumptions
- I intend to share considerations you may find helpful in your role

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## What Are the Assumptions in This Study for LEOFF 2?

| Assumption                   | Use of Assumption  |
|------------------------------|--|
| <b>Inflation</b>             | Model post-retirement COLAs based on changes in Consumer Price Index (CPI) for Seattle, Tacoma, Bellevue (STB)<br>Building block for other assumptions |
| <b>General Salary Growth</b> | Project salaries to determine future retirement benefits and contribution rates as a percentage of payroll   |
| <b>Investment Return</b>     | Determine today's value of future benefit payments and salaries  |

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## What's the Purpose of These Assumptions?

- Used to measure pension obligations and determine contribution rates
  - Assumptions for an actuarial funding valuation
- No prescribed assumptions for financial reporting
  - Accounting valuations based on OSA's best estimate rate of investment return

## How Long Are the “Long-Term” Assumptions?

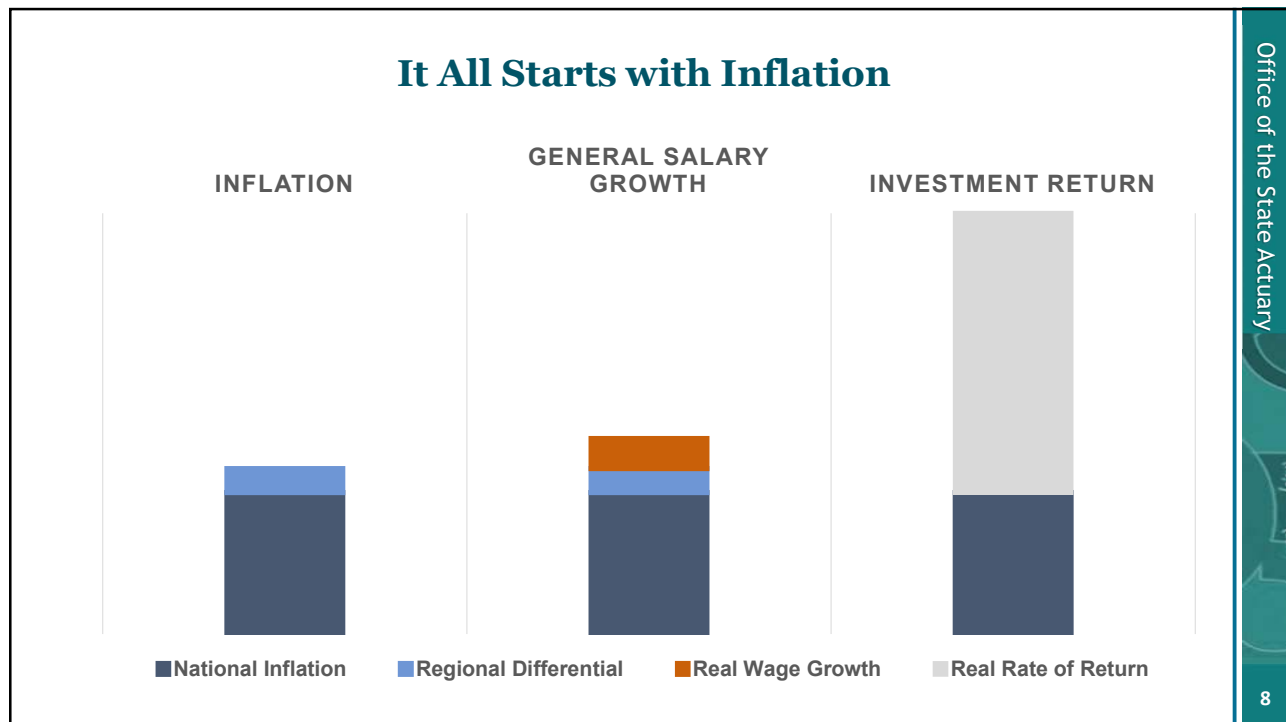
- Recommendations for each assumption are set with consideration for the relevant time horizon for an actuarial valuation
- Referred to as “duration”
  - Represents the weighted average length of plan liabilities and salaries; weighted by their present value

## Current Duration Measurements

| Duration by Open and Closed Plans<br>(As of 2019 Actuarial Valuation Report) |      |
|--|------|
| Duration of Liabilities  |      |
| <b>Open Plans</b>  | 20.7 |
| LEOFF 2 Only   | 22.0 |
| <b>Closed Plans</b>  | 8.1  |
| Duration of Salaries   |      |
| <b>Open Plans</b>  | 8.2  |
| LEOFF 2 Only   | 8.8  |

## How Do You Select Long-Term Economic Assumptions?

- Actuaries follow the guidance from applicable Actuarial Standards of Practice or ASOPs
- ASOP Number 27 provides guidance on the selection of economic assumptions and identifies the following summarized process
  - Identify components, if any, of the assumption
  - Evaluate relevant data
  - Consider factors specific to the measurement
  - Consider other general factors; and
  - Select a reasonable assumption
- Involves a fair amount of professional judgment
  - Education and experience



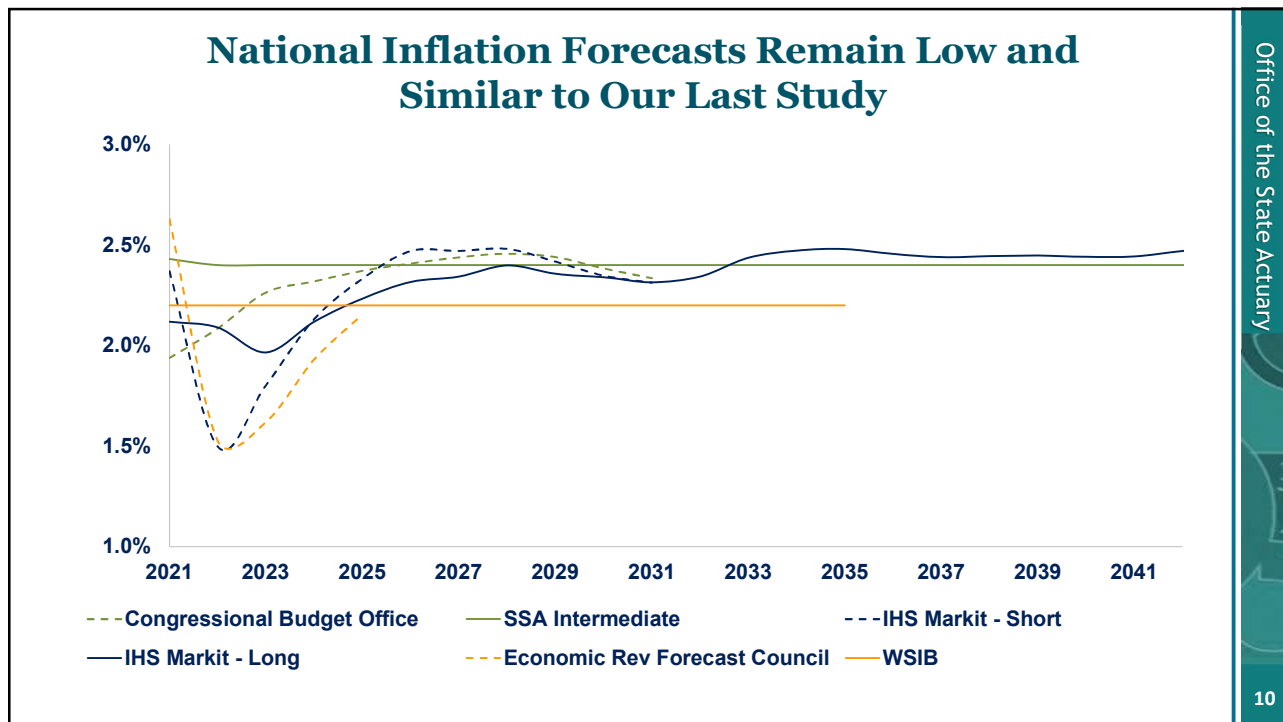
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### What Is Relevant Data for Setting These Assumptions?

- While we review historical data, we mostly rely on relevant forecasts
- These assumptions are intended to estimate the future, not replicate the past
- The conditions of the past may not be present today
- Consistent with purpose/use of these assumptions, we put more weight on long-term than short-term forecasts

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### We Continue to Expect STB Inflation to Outpace National Inflation

|                      | Average Inflation |                   |            |
|----------------------|-------------------|-------------------|------------|
|                      | STB<br>CPI-W      | National<br>CPI-W | Difference |
| <b>Last 30 years</b> | 2.72%             | 2.26%             | 0.46%      |
| <b>Last 25 years</b> | 2.52%             | 2.11%             | 0.42%      |
| <b>Last 20 years</b> | 2.36%             | 2.03%             | 0.34%      |
| <b>Last 15 years</b> | 2.39%             | 1.87%             | 0.52%      |
| <b>Last 10 years</b> | 2.27%             | 1.66%             | 0.62%      |
| <b>Last 5 years</b>  | 2.60%             | 1.70%             | 0.90%      |

■ Consistent with our prior study, we continue to assume a 0.40% regional price inflation differential

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## What about the Higher Levels of Inflation We're Experiencing Today?

- Inflation in 2021 has been significantly higher than recent years, but we believe it will be transitory
- Consistent with current Federal Reserve position
  - Acknowledge that inflation is higher than 2% target now
  - “Time will tell whether we have reached 2% inflation on a sustainable basis” - Chair Powell
  - “Today we see little evidence of wage increases that might threaten excessive inflation” - Chair Powell
- Latest commentary on inflation from Washington ERFC
  - The increase in inflation this year [2021] is expected to be temporary
  - Much of the recent increase in prices is due to the recovery of prices of services driven down during the pandemic
  - Constraints on supply chains have also impacted prices

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## OSA Models Total Salary Growth with Economic and Demographic Assumptions

- Economic assumption
  - Inflation
  - Real Wage Growth (economic growth above inflation)
- Demographic assumption
  - Service-Based Salary increases
  - For example, merit, longevity or “step increases”
  - Studied every 5-6 years as part of the *Demographic Experience Study*
- We combine all sources, economic and demographic, to model total expected salary growth
- Focusing on the economic assumption today
  - Once you set your Inflation assumption, you're left with the Real Wage Growth assumption to set your General Salary Growth assumption

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## An Example of Current Total Salary Growth Assumptions

| 2019 Total Expected Salary Growth—Current Assumptions |        |          |       |       |         |          |         |         |           |
|---|--------|----------|-------|-------|---------|----------|---------|---------|-----------|
| <i>(Dollars in Millions)</i>                          | PERS 1 | PERS 2/3 | PSERS | TRS 1 | TRS 2/3 | SERS 2/3 | LEOFF 1 | LEOFF 2 | WSPRS 1/2 |
| <b>Total Salary</b>                                   | 108.8  | 11,611.3 | 559.8 | 37.1  | 7,138.8 | 2,595.2  | 2.2     | 2,234.7 | 114.9     |
| <b>Expected Growth</b>                                | 3.87%  | 5.27%    | 5.74% | 3.74% | 5.50%   | 5.82%    | 3.52%   | 5.55%   | 5.30%     |

- 2.75% assumed inflation and 0.75% assumed real wage growth under current assumptions
- For LEOFF 2, that leaves about 2%, on average, for service-based salary increases in 2019

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## We've Observed a Longer-Term Downward Trend in Historical General Salary Growth, Inflation, and Real Wage Growth

| Estimated General Salary Growth          |   |                        |                                |
|--|---|------------------------|--------------------------------|
| Employees in Open DRS Administered Plans |   |                        |                                |
|  | Observed Growth of Average Salary (a + b) | Observed Inflation (a) | Estimated Real Wage Growth (b) |
| <b>Geometric Averages</b>                |   |                        |                                |
| Last 10 years (2010-2019)                | 2.73%                                     | 2.17%                  | 0.56%                          |
| Last 20 years (2000-2019)                | 3.38%                                     | 2.46%                  | 0.92%                          |
| Last 30 years (1990-2019)                | 3.60%                                     | 2.90%                  | 0.69%                          |

- Observed Growth of Average Salary = Observed Inflation + Estimated Real Wage Growth
- Estimated because we assume a stable population and cannot specifically identify and back-out service-based salary increases
- We do not rely on LEOFF 2 data only for this assumption; overstates observed real wage growth under this method

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## Decrease in Forecasted National Real Wage Growth since Our Last Study

- We review national forecasts from the CBO and SSA to determine if forecasted productivity or real wage growth has changed since our last study
- However, we do not rely on these specific forecasts (point estimates) when recommending a General Salary Growth assumption
  - National forecasts rely on a broader definition of wages which can include benefits
  - CBO and SSA forecasts for real wage growth include all sources of increase above inflation (including demographic sources)
  - In contrast, OSA models inflation, real wage growth, and service-based salary increases
- CBO and SSA average annual real wage growth forecasts for the next 10 years, declined by 11-13% from our last study

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## What about the Potential for Short-Term Above-Expected Wage Increases?

- A possible outcome
- Our General Salary Growth assumption represents average annual growth over the measurement period
  - Not intended to forecast a single year's wage growth
- As we have done in the past, if we observe actual salary growth well below or well above our longer-term expectations, we will update our assumptions in a future actuarial valuation
  - For example, an adjustment to a single year of projected salary growth based on known/adopted salary increases
  - An assumption change to reflect known but not yet reflected salary data after the measurement date of the valuation

17



## What Are Some of the Key Considerations When Selecting a Return Assumption?

- Capital Market Assumptions or CMAs
- Asset allocation
- Simulated future returns, net of expenses
- Sensitivity analysis
- Consistency of WSIB CMAs and return simulations with use for setting assumptions for a pension funding valuation

18

## What Are Capital Market Assumptions?

- According to WSIB, CMAs are the cornerstone in the development of a strategic asset allocation strategy
- Represent the projected behavioral characteristics of asset classes in terms of
  - Risk (volatility)
  - Reward (return)
  - Relationship (correlation)
- WSIB CMAs developed for a 15-year time horizon
- Not developed for the purpose of setting actuarial assumptions, but can inform the selection of actuarial assumptions

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## WSIB CMAs Have Changed since Our Last Study

| WSIB Portfolio Statistics & Capital Market Assumptions |                        |       |            |                    |       |            |
|--|------------------------|-------|------------|--------------------|-------|------------|
| Asset Class  | Expected 1-Year Return |       |            | Standard Deviation |       |            |
|  | 2021                   | 2019  | Difference | 2021               | 2019  | Difference |
| Global Equity  | 8.1%                   | 8.5%  | (0.4%)     | 19.0%              | 18.5% | 0.5%       |
| Tangible Assets  | 6.9%                   | 7.3%  | (0.4%)     | 12.0%              | 13.0% | (1.0%)     |
| Fixed Income   | 3.7%                   | 4.4%  | (0.7%)     | 6.0%               | 6.0%  | 0.0%       |
| Private Equity   | 11.1%                  | 11.5% | (0.4%)     | 25.0%              | 25.0% | 0.0%       |
| Real Estate  | 7.6%                   | 8.0%  | (0.4%)     | 13.0%              | 14.0% | (1.0%)     |
| Cash   | 1.7%                   | 2.6%  | (0.9%)     | 1.5%               | 1.5%  | 0.0%       |

- 1-year expected returns decreased across all asset classes
- Mixed changes to expected standard deviation (or volatility)

20

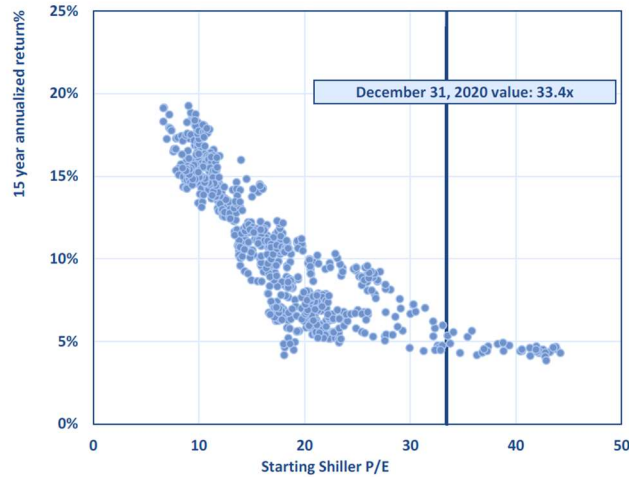
## Why Could We Expect Lower Future Returns?

- In general, financial assets represent future cash flow
  - Equities generally represent future earnings and dividends (where applicable)
  - Fixed income generally represents future coupon payments and the ultimate repayment of principal
  - Real estate can represent future lease payments
- Markets put a price on expected future cash flow and perceived level of risk
  - Those prices vary by the asset classes listed above
- A discount rate that equates the current price with the expected future cash flow is the expected return
- Lower/higher prices come from higher/lower discount rates
- Lower/higher prices imply higher/lower future returns

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## An Example of Why We Could Expect Lower Future U.S. Equity Returns

Starting Shiller P/E and Subsequent 15-Year U.S. Equity Return



Source: Robert Shiller

## CTF Asset Allocation Unchanged since Our Last Study

| WSIB Target Asset Allocation |             |             |            |
|------------------------------|-------------|-------------|------------|
|                              | 2021        | 2019        | Difference |
| Global Equity                | 32%         | 32%         | 0%         |
| Tangible Assets              | 7%          | 7%          | 0%         |
| Fixed Income                 | 20%         | 20%         | 0%         |
| Private Equity               | 23%         | 23%         | 0%         |
| Real Estate                  | 18%         | 18%         | 0%         |
| Cash                         | 0%          | 0%          | 0%         |
| <b>Total</b>                 | <b>100%</b> | <b>100%</b> |            |

- A future change in the CTF asset allocation could lead to a different recommended return assumption in the future

## WSIB Simulated Returns for the CTF Have Decreased since Our Last Study

| Simulated Future Investment Returns* |      |      |            |
|--------------------------------------|------|------|------------|
|                                      | 2021 | 2019 | Difference |
| 75th Percentile                      | 8.8% | 9.3% | (0.5%)     |
| 60th Percentile                      | 7.6% | 8.1% | (0.5%)     |
| 55th Percentile                      | 7.2% | 7.7% | (0.5%)     |
| Median Return                        | 6.9% | 7.4% | (0.5%)     |
| 45th Percentile                      | 6.5% | 7.0% | (0.5%)     |
| 40th Percentile                      | 6.1% | 6.6% | (0.5%)     |
| 25th Percentile                      | 4.9% | 5.4% | (0.5%)     |

\*Simulated returns over 25-year period.

- 50 basis point decreases to the median return (and at most percentiles)
- Half the simulated returns fall below (or above) “Median Return”
- We focus on the median when setting this assumption
- Corresponds to a similar decrease in assumed returns by asset class

## Simulated Returns Vary with Use of Different CMAs

| 25-Year Estimated Median Return Sensitivity |      |                                |      |                               |      |
|---|------|--------------------------------|------|-------------------------------|------|
|   | Base | Private Equity Expected Return |      | Global Equity Expected Return |      |
|   |      | (1%)                           | 1%   | (1%)                          | 1%   |
| Median Return                               | 6.9% | 6.7%                           | 7.1% | 6.6%                          | 7.2% |

- Modeled a decrease or increase in the expected 1-year return of private equities and global equities by 1%
- These two asset classes comprise 55% of the asset allocation of the CTF
- Median returns over 25 years fall below the current LEOFF 2 assumption of 7.4% with a 1% increase in 1-year returns for either asset class

## Other Considerations before Recommending a Return Assumption

- Consistency of WSIB CMAs and return simulations with use for setting assumptions for a pension funding valuation
  - OSA assumes higher national inflation than WSIB CMAs
  - Time horizons vary between CMAs and retirement system plan durations
- Differences can lead to adjusted return expectations for pension funding

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## Summary of Long-Term Economic Assumptions

| Assumption               | Current | Recommended |
|--------------------------|---------|-------------|
| Inflation                | 2.75%   | 2.75%       |
| General Salary Growth    | 3.50%   | 3.25%       |
| Annual Investment Return | 7.40%   | 7.00%       |

- We developed these assumptions as a consistent set of economic assumptions and recommend reviewing them as a set of assumptions
  - Changing the Inflation assumption, for example, without changing the Salary Growth or nominal Investment Return assumptions could lead to an inconsistent set of assumptions
- Adopting recommendation will decrease the plan's funded status in the short-term and increase minimum contribution rates

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## Funded Status Impact – Preliminary

| Change in Funded Ratio (FR)—Preliminary |                           |                           |                           |                           |
|---|---------------------------|---------------------------|---------------------------|---------------------------|
|   | As of<br>June 30,<br>2019 | As of<br>June 30,<br>2021 | As of<br>June 30,<br>2023 | As of<br>June 30,<br>2025 |
| <b>Baseline Projection</b>              | <b>111%</b>               | <b>113%</b>               | <b>113%</b>               | <b>113%</b>               |
| FY 2021 Return (a)                      | 0%                        | 3%                        | 10%                       | 17%                       |
| New Assumptions (b)                     | (6%)                      | (6%)                      | (7%)                      | (7%)                      |
| <b>Total Change (a + b)</b>             | <b>(6%)</b>               | <b>(3%)</b>               | <b>4%</b>                 | <b>9%</b>                 |
| <b>New Projected FR</b>                 | <b>105%</b>               | <b>110%</b>               | <b>117%</b>               | <b>123%</b>               |

*Note: Preliminary values subject to change. Actual results may also vary from these preliminary values. Baseline Projection under current assumptions and returns through June 30, 2020.*

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## Change In Minimum Contribution Rates – Preliminary

| Change in Total Employer Projected Contribution Rates—Preliminary |                     |                     |                     |
|---|---------------------|---------------------|---------------------|
|   | 2021-23<br>Biennium | 2023-25<br>Biennium | 2025-27<br>Biennium |
| <b>Baseline Projection</b>  | <b>8.53%</b>        | <b>8.53%</b>        | <b>7.74%*</b>       |
| 90% Minimum rate  |                     | 7.71%               | 7.74%               |
| 100% Minimum rate   |                     | 8.57%               | 8.60%               |
| <b>New Projected Rate</b>   | <b>8.53%</b>        | <b>8.53%</b>        | <b>8.30%*</b>       |
| 90% Minimum rate  |                     | 8.27%               | 8.30%               |
| 100% Minimum rate   |                     | 9.18%               | 9.23%               |

*Note: Rates through 2023-25 adopted by the Board and assumed to remain unchanged. Preliminary values subject to change. Actual results may also vary from these preliminary values. Baseline Projection under current assumptions. New Projected Rate under recommended assumptions.*

*\*Represents a minimum contribution rate at 90% of the Entry Age Normal Cost rate.*

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## Concluding Remarks

- Funded status impacts from adopting a lower return assumption represent short-term impacts required to offset lower expected long-term investment returns
- Long-term funded status impact will depend on actual experience
- Expected funded status through June 30, 2025, remains at least 105% under recommended assumptions
  - Actual funded status may vary
- Based on the *2019 Actuarial Valuation Report*, all the current economic assumptions are reasonable
- Other State's Economic Assumptions and Historical Washington State Assumptions in the Appendix

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## Questions?



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**Questions? Please Contact: The Office of the State Actuary**  
**[leg.wa.gov/OSA](http://leg.wa.gov/OSA); [state.actuary@leg.wa.gov](mailto:state.actuary@leg.wa.gov)**  
**360-786-6140, PO Box 40914, Olympia, WA 98504**  
**Matthew M. Smith**

O:\LEOFF 2 Board\2021\09.29\State.Actuaries.Rec.Long.Term.Econ.Assumptions.pptx



# Thank You

Office of the State Actuary  
"Supporting financial security for generations."

September 29, 2021

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## Appendix

- Other States' Economic Assumptions
- Historical Economic Assumptions for Washington State Pension Systems



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## Other States' Economic Assumptions

| Economic Assumptions for Selected Plans Outside Washington <sup>1</sup> |                   |                       |                               |           |
|---|-------------------|-----------------------|-------------------------------|-----------|
| Plan Name   | Investment Return | General Salary Growth | Real Wage Growth <sup>2</sup> | Inflation |
| WA 2021 Economic Experience Study Recommendation                        | 7.00%             | 3.25%                 | 0.50%                         | 2.75%     |
| WA Currently Prescribed Economic Assumptions                            | 7.50%             | 3.50%                 | 0.75%                         | 2.75%     |
| Alaska PERS   | 7.38%             | 2.75%                 | 0.25%                         | 2.50%     |
| Alaska Teachers   | 7.38%             | 2.75%                 | 0.25%                         | 2.50%     |
| California PERS   | 6.80%             | 2.75%                 | 0.25%                         | 2.50%     |
| California Teachers   | 7.00%             | 3.50%                 | 0.75%                         | 2.75%     |
| Colorado PERA   | 7.25%             | 3.00%                 | 0.70%                         | 2.30%     |
| Florida Retirement System   | 7.00%             | 3.25%                 | 0.85%                         | 2.40%     |
| Idaho PERS  | 6.30%             | 3.75%                 | 0.75%                         | 2.30%     |
| Iowa PERS   | 7.00%             | 3.25%                 | 0.65%                         | 2.60%     |
| Missouri State Employees  | 6.95%             | 2.50%                 | 0.25%                         | 2.25%     |
| Ohio PERS   | 7.20%             | 3.25%                 | 0.75%                         | 2.50%     |
| Oregon PERS   | 6.90%             | 3.50%                 | 1.00%                         | 2.50%     |
| Wisconsin Retirement System   | 5.40%             | 3.00%                 | 0.50%                         | 2.50%     |
| Selected Public Plans Outside WA – Average                              | 6.88%             | 3.10%                 | 0.58%                         | 2.47%     |
| Selected Public Plans Outside WA – Minimum                              | 5.40%             | 2.50%                 | 0.25%                         | 2.25%     |
| Selected Public Plans Outside WA – Maximum                              | 7.38%             | 3.75%                 | 1.00%                         | 2.75%     |

Note: We updated the Investment Return assumptions, in red, for California PERS, Idaho PERS, and Oregon PERS based on more recent information than what was used in our 2021 Report on Financial Condition and Economic Experience Study.

<sup>1</sup>Data gathered from NASRA, the Public Plans Database maintained by the Center for Retirement Research, and individual system Annual Comprehensive Financial Reports or Actuarial Valuations as of June 30, 2021. Where more recent updates were available (e.g., via press release issued after the last report), that information was used. For systems having multiple benefit tiers with different assumptions, the largest was used.

<sup>2</sup>For comparison to our economic assumptions, we assumed Real Wage Growth was the difference between General Salary Growth and Inflation.

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## Other States' Economic Assumptions – Select, Well Funded Peer Systems

| Economic Assumptions for Selected Plans Outside Washington <sup>1</sup> |                    |                       |                               |                    |
|---|--------------------|-----------------------|-------------------------------|--------------------|
| Plan Name   | Investment Return  | General Salary Growth | Real Wage Growth <sup>2</sup> | Inflation          |
| WA 2021 Economic Experience Study Recommendation                        | 7.00%              | 3.25%                 | 0.50%                         | 2.75%              |
| WA Currently Prescribed Economic Assumptions                            | 7.50%              | 3.50%                 | 0.75%                         | 2.75%              |
| Idaho PERS  | 6.30%              | 3.75%                 | 0.75%                         | 2.30%              |
| Nebraska NPERs  | 7.30% <sup>3</sup> | 3.15% <sup>3</sup>    | 0.50%                         | 2.65% <sup>3</sup> |
| New York NYSLRS-ERS   | 5.90%              | 4.40%                 | 1.70%                         | 2.70%              |
| South Dakota SDRS   | 6.50%              | 5.25%                 | 3.00%                         | 2.25%              |
| Tennessee   | 7.25%              | 3.00%                 | 0.50%                         | 2.50%              |
| Wisconsin Retirement System   | 5.40%              | 3.00%                 | 0.50%                         | 2.50%              |
| Selected Public Plans Outside WA – Average                              | 6.44%              | 3.76%                 | 1.16%                         | 2.48%              |
| Selected Public Plans Outside WA – Minimum                              | 5.40%              | 3.00%                 | 0.50%                         | 2.25%              |
| Selected Public Plans Outside WA – Maximum                              | 7.30%              | 5.25%                 | 3.00%                         | 2.50%              |

Note: Selected systems had a funded status of at least 90% in the most recent PEW State Pension Funding Gap report.

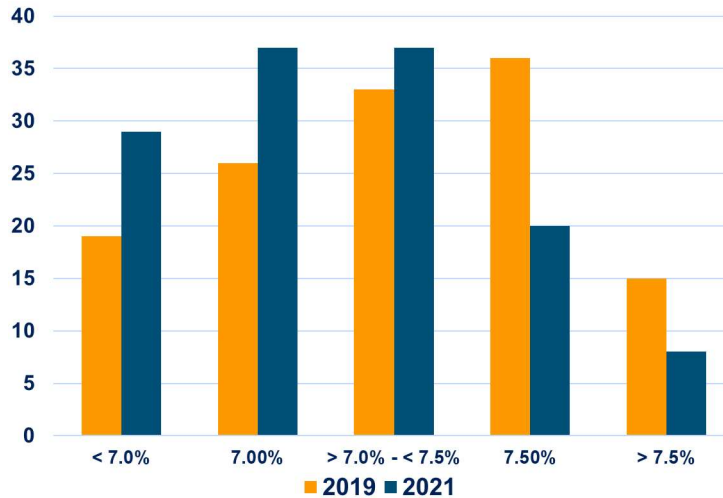
<sup>1</sup>Data gathered from NASRA, the Public Plans Database maintained by the Center for Retirement Research, and individual system Annual Comprehensive Financial Reports or Actuarial Valuations as of June 30, 2021. Where more recent updates were available (e.g., via press release issued after the last report), that information was used. For systems having multiple benefit tiers with different assumptions, the largest was used.

<sup>2</sup>For comparison to our economic assumptions, we assumed Real Wage Growth was the difference between General Salary Growth and Inflation.

<sup>3</sup>Investment Return grading down to 7.0% by 2024. General Salary Growth grading down to 2.85% by 2024. Inflation grading down to 2.35% by 2024.

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### Distribution of Return Assumptions in Other States



Median return declined from 7.25% to 7.0%

Source: NASRA Public Fund Survey. Does not reflect updates noted on slide 34.

### Historical Economic Assumptions for Washington State Pension Systems

| Historical Economic Assumptions for Washington State Pension Systems |                                  |                                    |           |                                    |                                      |
|--|----------------------------------|------------------------------------|-----------|------------------------------------|--------------------------------------|
| Valuation Years  | Investment Return                | General Salary Growth              | Inflation | Real Wage Growth                   | Membership Growth for Plan 1 Funding |
| 1989 - 1994  | 7.50%                            | 5.50%                              | 5.00%     | 0.50%                              | 0.75% TRS<br>1.25% PERS              |
| 1995 - 1997  | 7.50%                            | 5.00%                              | 4.25%     | 0.75%                              | 0.90% TRS<br>1.25% All Others        |
| 1998 - 1999  | 7.50%                            | 4.00%                              | 3.50%     | 0.50%                              | 0.90% TRS<br>1.25% All Others        |
| 2000 - 2008  | 8.00%                            | 4.50%                              | 3.50%     | 1.00%                              | 0.90% TRS<br>1.25% All Others        |
| 2009 - 2010  | 8.00%                            | 4.50% LEOFF 2<br>4.00% Other Plans | 3.50%     | 1.00% LEOFF 2<br>0.50% Other Plans | 0.90% TRS<br>1.25% All Others        |
| 2011 - 2012  | 7.5% LEOFF 2<br>7.9% Other Plans | 3.75%                              | 3.00%     | 0.75%                              | 0.80% TRS<br>0.95% PERS              |
| 2013 - 2014  | 7.5% LEOFF 2<br>7.8% Other Plans | 3.75%                              | 3.00%     | 0.75%                              | 0.80% TRS<br>0.95% PERS              |
| 2015   | 7.5% LEOFF 2<br>7.7% Other Plans | 3.75%                              | 3.00%     | 0.75%                              | 0.80% TRS<br>0.95% PERS              |
| 2016   | 7.5% LEOFF 2<br>7.7% Other Plans | 3.75%                              | 3.00%     | 0.75%                              | 1.25% TRS<br>0.95% PERS              |
| 2017 - 2018  | 7.4% LEOFF 2<br>7.5% Other Plans | 3.50%                              | 2.75%     | 0.75%                              | 1.25% TRS<br>0.95% PERS              |
| 2019 - 2020  | 7.4% LEOFF 2<br>7.5% Other Plans | 3.50%                              | 2.75%     | 0.75%                              | 1.25% TRS<br>0.95% PERS              |



Annual AGO Training Presentation  
September 29, 2021  
AAG Tor Jernudd



## AGENDA

- 1) Board of Trustees Fiduciary Duty  
A Historical Perspective
- 2) Training Refresher / Reminders

- **RCW 41.26.705**

- **Intent—2003 c 2.**

- It is the intent of chapter 2, Laws of 2003 to:

- (1) Establish **a board of trustees** responsible for the adoption of actuarial standards to be applied to the plan;

- (2) Provide for additional benefits for firefighters and law enforcement officers subject to the cost limitations provided for in chapter 2, Laws of 2003;

- (3) Exercise **fiduciary** responsibility in the oversight of those pension management functions assigned to the board;

*And paraphrasing.....authorizes the board to perform a bunch of relatively specific things.*



Why **a board of trustees** ?

Why **fiduciary** ?

Why **a board of trustees** ?

Why **fiduciary** ?

*What do the words mean?*

*Where do the concepts come from?*

*What purpose do they serve?*

*How have they evolved?*



OXFORD DEFINITIVE DICTIONARY OF THE ENGLISH LANGUAGE

Board - A group of people constituted as the decision-making body of an organization.







OXFORD DEFINITIVE DICTIONARY OF THE ENGLISH LANGUAGE

**Trustees** - An individual person or member of a board given control or powers of administration of property in trust with a legal obligation to administer it solely for the purposes specified.



trust (n.)

Image of current LEOFF 2  
Board Member

c. 1200, "reliance on the veracity, integrity, or other virtues of someone or something; religious faith," from Old Norse traust "help, confidence, protection, support,"

**Fiduciary** - agent legally responsible for managing property for the benefit of another individual or a group.



In Roman law, **fiducia** was "a right transferred in trust;" paper currency sense (1878) is because its value depends on the trust of the public. As a noun, "one who holds something in trust," from 1630s.

Image of a Roman  
Era dog

Fido



Board – why “a group” and not an individual



## Board – why “a group” and not an individual

Continuity

Collective skill and wisdom

Representative democracy

Collective accountability / TRUST



## **Fiduciary / Trust**

Core concept / purpose: to Administer Property of Another

First Written Record: Hammurabi's laws

Image of  
Hammurabi's  
tablet



**Fiduciary / Trust**

Image representing  
Crusades



Fiduciary / Trust

Image of 15<sup>th</sup> century  
Sailing vessel

Image of Dutch East India Company  
Logo on Coinage



Fiduciary / Trust

Image of Frans Hals Painting with council of 5 Dutch Ladies





Fiduciary / Trust

Image of Child King



Fiduciary / Trust

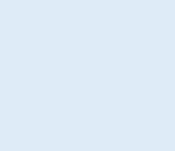
Image of transcontinental railroad  
Postage stamp



Fiduciary / Trust

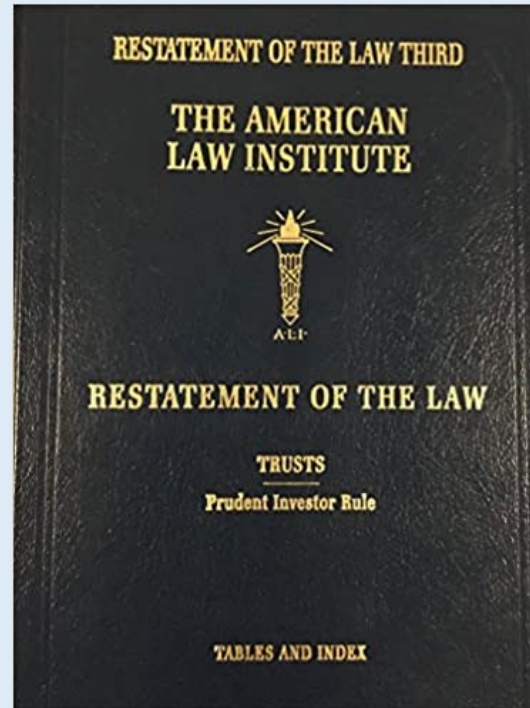


Image of Otto Bismarck





## Fiduciary / Trust



## FUNDAMENTAL FIDUCIARY DUTIES

1. *Primary Loyalty Rule* – Duty to act in the best collective interests of the plans that entrust their assets in this Board's care; not to promote personal or others' interests
2. *Exclusive Benefit Rule* – Duty to use assets solely for the ultimate purpose of paying the members' promised benefits and *reasonable* administrative expenses
3. *Prudence Standard* – Duty to act with the care , skill, prudence and diligence under the prevailing circumstances of a prudent person "in a like capacity and familiar with these matters...in the conduct of an enterprise of like character and with like aims"
4. *Diversification* – N/A
5. *Follow the Plan Documents* – Duty to administer the Plan in accordance with the Plan documents – including state and federal law, IRC and regulations, Board charters and policies.



## Potential Fiduciary Potholes

Flawed board governance

Inability to act collectively as a single fiduciary

Inattention to changing circumstances

Flawed processes establishing responsibility and accountability

Delay

Conflicts of interest

Undue external influence

Inability to attract and retain qualified investment staff



# Guiding Principles of Fiduciary Duty

Integrity

Fairness

Balance

Prudence

Collaboration



## PART II REFRESHER

- 1) LEOFF 2 Enabling Statute
- 2) Ethics Laws
- 3) Public Records Act
- 4) Open Public Meetings Act
- 5) Other Resources
- 6) Gut check





## RCW 41.26.700-922 “Plan 2 Governance”



### "PLAN 2 GOVERNANCE"

- 41.26.700** Overview—Intent.
- 41.26.705** Intent—2003 c 2.
- 41.26.710** Definitions.
- 41.26.715** Board of trustees—Created—Selection of trustees—Terms of office—Vacancies.
- 41.26.7151** Board of trustees—Political party representation.
- 41.26.717** Additional duties and powers of board.
- 41.26.720** Board of trustees—Powers—Meeting procedures—Quorum—Judicial review—Budget.
- 41.26.725** Board of trustees—Contributions—Minimum and increased benefits.
- 41.26.730** Joint committee on pension policy—Pension funding council.
- 41.26.732** Plan 2 expense fund—Board oversight and administration—State investment board.
- 41.26.735** Asset management.
- 41.26.740** Reimbursement for expenses.
- 41.26.802** Local law enforcement officers' and firefighters' retirement system benefits improvement account—Transfer into account.
- 41.26.805** Local law enforcement officers' and firefighters' retirement system benefits improvement account—Creation—Use—Administration—Inv
- 41.26.904** Effective date—2003 c 2 (Initiative Measure No. 790).
- 41.26.906** Effective date—2003 c 92.
- 41.26.921** Effective date—1977 ex.s. c 294.
- 41.26.922** Construction—Chapter applicable to state registered domestic partnerships—2009 c 521.



# Chapter 42.52 RCW ETHICS IN PUBLIC SERVICE

Gifts

Employment and other conflicts

No privileges / other compensation

State Resources



## Chapter 42.56 RCW PUBLIC RECORDS ACT

“The people...do not give their public servants the right to decide what is good for the people to know and what is not good for them to know. ...This chapter shall be ***liberally construed*** and its exemptions narrowly construed...”

EMAIL TEXTS IM VOICEMAIL / RECORDINGS PHOTOS SOCIAL MEDIA INTERNET

Records Retention Policies

Reasonable Searches

Boundaries



## Chapter [42.30](#) RCW OPEN PUBLIC MEETINGS ACT

It is the intent of this chapter that their actions be taken openly and that their deliberations be conducted openly. ...The people insist on remaining informed so that they may retain control over the instruments they have created.

### **Cautions**

Accidental Meetings

Hub Spoke

Reply All

Quorum / Collective Intent /Transact Business



# Other Resources

LEOFF 2 Staff

AAG

Other State Resources

Own staff



# **Gut Check Guiding Principles of Fiduciary Duty**

Integrity

Fairness

Balance

Prudence

Collaboration



## PART II REFRESHER

- 1) LEOFF 2 Enabling Statute
- 2) Ethics Laws
- 3) Public Records Act
- 4) Open Public Meetings Act
- 5) Other Resources
- 6) Gut check

QUESTIONS?

**BOARD OPERATING POLICY - RULE 6. ELECTION AND DUTIES OF OFFICERS**

- a. The Board shall elect a Chairman and Vice-Chairman from its membership. Nominations for Chairman and Vice-Chairman shall be open during the regularly scheduled board meeting held in August. Any member may verbally nominate another member or themselves when the presiding officer declares the nominating period open. Elections for Chairman and Vice-Chairman shall be held during the regularly scheduled September board meeting. Terms for Chairman and Vice-Chairman shall be for a period of two years commencing immediately following the officers' election.
- b. Both Chairman and Vice-Chairman shall be members of the Administrative Committee. One additional member shall be chosen by board members representing employer groups. Administrative Committee members shall serve two-year terms that begin and end with the Chairman and Vice-Chairman's terms.
- c. The Chair shall preside at all meetings of the Board and Administrative Committee, except that the Vice Chair shall preside when the Chair is not present. In their absence, an Administrative Committee member may preside.
- d. Board staff shall prepare and maintain a record of the proceedings of all meetings of the Board and subcommittees of the Board.
- e. The Administrative Committee shall perform all duties delegated by the Board. The Administrative Committee shall coordinate the annual evaluation of the Executive Director of the agency. (Policy 1 – Executive Director Performance Evaluation)
- f. Board members shall consult with the Executive Director before referring issues to the Assistant Attorney General so that any budget constraints may be taken into consideration. Advice from the Attorney General's Office to the Board may be subject to the attorney client privilege. When subject to the privilege, Board members are advised to maintain the advice as confidential. The privilege may be waived only by vote of the Board.
- g. The Executive Director may refer requests for information or services by Board members that are directly related to current Board projects or proposals and/or require a significant use of staff resources to either the Chair or the Administrative Committee.
- h. Such requests will be approved by either the Chair or by a majority vote of the Administrative Committee prior to action by staff. The Chair or Administrative Committee will consider priorities of all current projects and budget constraints in making this decision.
- i. Any Board member may attend Administrative Committee meetings at any time, though participation may be restricted for time or procedural purposes.





# Board Officer Elections

September 29, 2021

# Board Officer Elections

- **Chairman\***
- **Vice-Chairman\***
- **Administrative Committee: One member representing employer groups**

\*Chairman and Vice-Chairman are members of the Administrative Committee by policy



Thank You



September 29, 2021

## Interruptive Military Service Credit

### COMPREHENSIVE FOLLOW-UP REPORT

By Jacob White

Senior Research & Policy Manager

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## ISSUE STATEMENT

Eligibility for no-cost interruptive military service credit is limited to service where a campaign medal was earned and does not include service where an expeditionary medal was earned.

## OVERVIEW

LEOFF Plan 2 members may establish service credit for military service interrupting their LEOFF service. Member contributions are waived for LEOFF Plan 2 members whose interruptive military service was: 1) during a period of war; or 2) during a specified conflict for which they earned a campaign badge or medal.

## BACKGROUND AND POLICY ISSUES

### General Background

Interruptive military service credit applies to all Washington State retirement systems, including LEOFF Plan 2. A member qualifies for this benefit when they take a leave of absence from a DRS covered position to serve in the United States military, and the member returns to employment with their employer within 90 days of being honorably discharged. When this occurs, membership in the retirement system is considered to be interrupted.

There are two types of pension benefits for interruptive military service: fully subsidized (“no-cost interruptive military service credit”) and partially subsidized (“reduced-cost interruptive military service credit”).

No-cost interruptive military service credit is awarded if the service took place during a period of war, or certain armed conflicts in which an approved campaign medal or badge was obtained. A member can qualify for up to five years of no-cost interruptive military service credit. The employer and state pay their contributions plus interest and the system subsidizes the member contributions and interest.

Partially subsidized interruptive military service credit is awarded if the service did not take place during a period of war, or an armed conflict in which an approved campaign medal was

obtained.<sup>1</sup> In order to receive partially subsidized credit, a member must have been honorably discharged from their service and unable to qualify for no-cost credit. A member can qualify for up to five years of partially subsidized military service credit. The member must pay the member contribution cost; however, the interest on the member contributions is subsidized by the Plan. The member has five years from when they return to work to pay their contributions or they must pay those contributions prior to retirement, whichever occurs first. After the member pays their contributions, the employer and state are billed for the employer contributions plus interest.

A member may receive a total of 10 years of interruptive military service credit (up to 5 years no-cost interruptive military service credit and up to 5 years of partially subsidized). The member must fully pay the required contributions within 5 years of reemployment.

### **Qualifying for No-Cost Interruptive Military Service Credit**

To qualify for no-cost interruptive military service credit the member's service must have been during a "period of war", as defined in RCW 41.04.005(2). "Period of war" is defined under this statute as:

World War I; World War II; The Korean conflict; The Vietnam era<sup>2</sup>; The Persian Gulf War<sup>3</sup>; The period beginning on the date of any future declaration of war by the congress and ending on the date prescribed by presidential proclamation or concurrent resolution of the congress; and

Any armed conflicts, if the participant was awarded the respective campaign badge or medal, or if the service was such that a campaign badge or medal would have been awarded, except that the member already received a campaign badge or medal for a prior deployment during that same conflict.

The DoD awards a campaign badge or medal to service members who served during a specified conflict and were stationed in a designated war zone.<sup>4</sup>

Campaign medals, as defined by the DoD manual 1348.33 Volume 2, are medals which:

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<sup>1</sup> Responsibility for payment varies by the dates of service. If the military service was completed: Between October 1, 1977, and March 31, 1992, the member pays both the employer and member contributions plus interest; After March 31, 1992, and before October 6, 1994, the member pays the member contributions plus interest and the employer and state pay their contributions plus interest; After October 6, 1994, a member pays the member contributions (no interest) and the employer and state pays their contribution plus interest.

<sup>2</sup> Which means: The period beginning on February 28, 1961, and ending on May 7, 1975, in the case of a veteran who served in the Republic of Vietnam during that period; the period beginning August 5, 1964, and ending on May 7, 1975.

<sup>3</sup> Which was the period beginning August 2, 1990, and ending on February 28, 1991, or ending on November 30, 1995, if the participant was awarded a campaign badge or medal for such period.

<sup>4</sup> Defined conflicts include: the crisis in Lebanon, the invasion of Grenada, Operation Just Cause in Panama, Operation Restore Hope in Somalia, Operation Uphold Democracy in Haiti, Operation Joint Endeavor in Bosnia, Operation Noble Eagle, Operation Enduring Freedom in Southern or Central Asia, Operation Iraqi Freedom; Iraq and Syria, Operation Inherent Resolve; and Afghanistan, Operation Freedom's Sentinel.

“recognize service members who are deployed to the geographic area where the combat is actually occurring. Members awarded campaign medals have the highest degree of personal risk and hardship as they are conducting the combat operations and are deployed to the area where the combat is actually occurring.”

Interruptive military service that does not meet the definition of “period of war” does not qualify for no-cost interruptive military service credit. However, it does qualify for partially subsidized interruptive military service credit.

**Legislative History**

No-cost interruptive military service credit was created in 2009, with the passage of HB 1548. HB 1548 was endorsed by the SPP and the LEOFF Plan 2 Board. The legislative history of HB 1548 does not explicitly state the policy goals of the legislature in creating a no-cost interruptive military service credit benefit, or the reasons for placing the lines of demarcation between partially subsidized and no-cost interruptive military service credit at receiving a campaign badge.

In 2009, the LEOFF Plan 2 Board report<sup>5</sup> on this proposed benefit stated:

Arguments for eliminating the cost to the member include encouraging military service, supporting the ability to recruit military personnel into state/local government service, benefits (direct and indirect) to the State from military service rendered by public employees, recognition and support for Plan members serving the public at large in a high risk situation, and supplementing federal benefits which may be viewed as inadequate.

Some of the policy pros and cons of providing special or increased benefits to members based on military service, identified in presentations to the LEOFF Plan 2 Board and the SPP in 2008 and 2009, included:

| No Additional Benefits  | Additional Benefits   |
|---|---|
| Members serve voluntarily; no draft requires them to leave employment   | Encourage military service; help avoid need for a draft   |
| Members already receive adequate federal compensation and benefits for military service                         | Support ability to recruit more military personnel into state service and more state personnel into military service                  |
| Other members and employers would not have to absorb extra costs for these members                              | Support view that all WA citizens benefit, directly or indirectly, from military service rendered by public employees                 |
| More favorable service credit treatment is already given to these members (partially subsidized service credit) | Recognize that members who serve in conflicts are at higher risk for injury or death; pension Plans typically offer extra support for |

<sup>5</sup> [http://leoff.wa.gov/wp-content/uploads/2015/06/121708.6\\_Interruptive-Military-Service-Credit.pdf](http://leoff.wa.gov/wp-content/uploads/2015/06/121708.6_Interruptive-Military-Service-Credit.pdf)

|  |  |
|--|--|
|  | high risk occupations that serve the public at large             |
| Military service is unrelated to the service rewarded by state pension Plans | Supplement federal benefits, which may not be viewed as adequate |

During the 2017 legislative session, SB 5661 required the LEOFF Plan 2 Board to study interruptive military service credit for members not awarded a campaign badge or medal. The LEOFF Plan 2 Board completed that study during the 2017 interim and submitted the report to the legislature on January 1, 2018.

As a result of that study the LEOFF Plan 2 Board endorsed legislation (HB 2701) in 2018. This legislation added a provision to ensure that eligibility for no-cost interruptive military service credit for multiple deployments to the same conflict; added an end date in statute for the end of the Gulf War; and made two additional combat operations (Inherent Resolve, Iraq and Syria; and Freedom’s Sentinel, Afghanistan) eligible for no-cost interruptive military service credit. This legislation became effective June 7, 2018.

The statute which defines “period of war”, for purposes of not only receiving interruptive military service credit but also other non-pension benefits, has been amended eleven times since its adoption in 1969. The majority of these amendments have updated the list of periods of war and armed conflicts.

HB 2544 (2020) redefined “period of war” in RCW 41.04.005 to no longer identify specific conflicts and instead recognize all service from which a campaign badge or medal was earned. The LEOFF Plan 2 Board endorsed this legislation because it removes the need to amend “period of war” for each new conflict that qualifies for no-cost interrupt military service credit. HB 2544 (2020) also required the LEOFF Plan 2 Board and the Select Committee on Pension Policy to submit studies to the legislature on expanding the eligibility of no-cost interruptive military service credit. The Board voted to defer until next year making a recommendation to expand the no-cost interruptive military service credit benefit to service where the member earned an expeditionary medal. The Board expressed support of the policy to expand but also expressed concerns regarding the cost of the benefit and the expected state and local budget environment due to unknown revenue impacts from Covid-19.

**Department of Defense**

Campaign, Expeditionary, and Service (CE&S) medals recognize service members’ participation in military campaigns, expeditions, or other significant military operations, and for otherwise meritorious military service. Eligibility criteria for CE&S medals are based on a service member’s:

- Degree of personal risk (e.g., proximity to the enemy, service in a combat zone, imminent threat of hostilities);
- Degree of personal hardship;
- Participation in designated military operations; and,

- Extent of military service during specified time periods, duration, or types of duty.<sup>6</sup>

There are four categories of CE&S medals:

- **Campaign Medals** - Campaign medals recognize deployed participation in large-scale or long-duration combat operations. Campaign medals are associated with the highest level of personal risk and hardship. They are awarded to members who are deployed to the geographic areas where the combat is actually occurring. Service members deployed to areas where combat is occurring as a result of prolonged or large-scale military combat operations should be recognized with a separate and distinct campaign medal.
- **Expeditionary Medals** - Expeditionary medals recognize deployed participation in small scale and/or short-duration combat operations or military operations where there is an imminent threat of hostilities. Expeditionary medals are also awarded to members deployed in support of combat operations, but who are not in the geographic area where the actual combat is occurring. Expeditionary medals are associated with high levels of personal risk and hardship.
- **Deployed Service Medals** - Deployed service medals recognize deployment or assignment to a designated Area of Eligibility (AOE) to participate in, or directly support, a designated military operation where there is no foreign armed opposition or imminent threat of hostile action.
- **Individual Service Medals** - Individual service medals recognize individual merit, direct participation in a DoD approved military activity, undertaking, event or operation, or service during a specified period. Some individual service medals, such as the Prisoner of War (POW) medal, may recognize service involving significant personal risk and hardship, while others only recognize being in active military service during a particular period of time.<sup>7</sup>

Below is a table from the DoD Manual 1348.33, Volume 2, of current and recent CE&S medals:

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<sup>6</sup> DOD MANUAL 1348.33, VOLUME 2,  
[https://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodm/1348.33\\_Vol2.pdf?ver=2018-03-29-102726-900](https://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodm/1348.33_Vol2.pdf?ver=2018-03-29-102726-900)

<sup>7</sup> DOD MANUAL 1348.33, VOLUME 2,  
[https://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodm/1348.33\\_Vol2.pdf?ver=2018-03-29-102726-900](https://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodm/1348.33_Vol2.pdf?ver=2018-03-29-102726-900)



**Table 1: Categories of CE&S Medals**

| Title of Decoration <sup>1</sup>   | Sub-category of CE&S Medals |
|--|-----------------------------|
| Southwest Asia Service Medal <sup>2</sup>  | Campaign Medal              |
| Kosovo Campaign Medal  | Campaign Medal              |
| Afghanistan Campaign Medal   | Campaign Medal              |
| Iraq Campaign Medal  | Campaign Medal              |
| Inherent Resolve Campaign Medal  | Campaign Medal              |
| Armed Forces Expeditionary Medal   | Expeditionary Medal         |
| Global War on Terrorism Expeditionary Medal  | Expeditionary Medal         |
| Antarctic Service Medal  | Deployed Service Medal      |
| Armed Forces Service Medal   | Deployed Service Medal      |
| Korea Defense Service Medal  | Deployed Service Medal      |
| National Defense Service Medal   | Individual Service Medal    |
| Armed Forces Reserve Medal   | Individual Service Medal    |
| Humanitarian Service Medal   | Individual Service Medal    |
| Prisoner of War Medal  | Individual Service Medal    |
| Military Outstanding Volunteer Service Medal   | Individual Service Medal    |
| Global War on Terrorism Service Medal  | Individual Service Medal    |
| <p>Note 1: This list is not all-inclusive. Military Departments also have CE&amp;S medals (e.g., Navy Expeditionary Medal; Air Force Good Conduct Medal; Army Good Conduct Medal). Refer to each Military Department’s specific award guidance for additional information.</p> <p>Note 2: Before DoD established comprehensive CE&amp;S medal policy, the naming conventions for DoD CE&amp;S medals were inconsistent. This resulted in several medals with names that do not match the CE&amp;S medal category to which they are assigned.</p> |                             |

**LEOFF Plan 2 Interruptive Military Service Credit Data**

Between 2009 and 2019, 534 LEOFF Plan 2 members received no-cost interruptive military service credit. Those members received an average of 9.75 months of service credit.

During that same time period, 24 LEOFF Plan 2 members purchased partially subsidized interruptive military service credit. Those members purchased an average of 8.85 months of service credit. 40 LEOFF Plan 2 members requested a bill from DRS to purchase partially subsidized interruptive military service credit, but elected not to purchase the service credit. Those members would have received an average of 11.68 months of service credit.

**COST OF EXPANDING ELIGIBILITY**

In 2020 the Office of the State Actuary (OSA) completed an actuarial fiscal note for expanding no-cost interruptive military service credit to interruptive service where the member earned an expeditionary medal. OSA categorized the fiscal impacts prospectively (interruptive military service that occurs after the effective date of the bill) and retroactively (interruptive military service that occurred before the effective date of the bill). Below is a table from OSA of the contribution rate impact and the 25 year costs of the proposal:

| <b>(1) Prospective</b>              |                | <b>(2) Retroactive</b>              |                |
|-------------------------------------|----------------|-------------------------------------|----------------|
| <b>Impact on Contribution Rates</b> |                | <b>Impact on Contribution Rates</b> |                |
| <b>System/Plan</b>                  | <b>LEOFF 2</b> | <b>System/Plan</b>                  | <b>LEOFF 2</b> |
| <b>Current Members</b>              |                | <b>Current Members</b>              |                |
| Employee                            | 0.0013%        | Employee                            | 0.019%         |
| Employer                            | 0.0008%        | Employer                            | 0.012%         |
| State                               | 0.0005%        | State                               | 0.008%         |

| <b>25-Year Budget Impacts</b> |                | <b>25-Year Budget Impacts</b> |                |
|-------------------------------|----------------|-------------------------------|----------------|
| <i>(Dollars in Millions)</i>  | <b>LEOFF 2</b> | <i>(Dollars in Millions)</i>  | <b>LEOFF 2</b> |
| <b>2021-2046</b>              |                | <b>2021-2046</b>              |                |
| General Fund                  | \$0.3          | General Fund                  | \$4            |
| Non-General Fund              | 0.0            | Non-General Fund              | 0              |
| <b>Total State</b>            | <b>\$0.3</b>   | <b>Total State</b>            | <b>\$4</b>     |
| Local Government              | 0.4            | Local Government              | 5              |
| <b>Total Employer</b>         | <b>\$0.7</b>   | <b>Total Employer</b>         | <b>\$9</b>     |
| <b>Total Employee</b>         | <b>\$0.7</b>   | <b>Total Employee</b>         | <b>\$9</b>     |

*Note: Totals may not agree due to rounding.*

In December 2020, after OSA had completed their fiscal note, the LEOFF 2 Board received a response to a Freedom of Information Act request from the Department of Defense. IN preparation for this report OSA reviewed this data and provided the board with their initial analysis of the impacts of the data to their prior actuarial fiscal note analysis. Based on this new data set, OSA found that:

1. The ratio of Expeditionary-to-Campaign Medals could be lower than previously expected, potentially reducing the expected cost of this proposal by approximately 25 percent – both Prospective and Retroactive
2. At the same time, it appears that Expeditionary Medals were granted at a higher rate in the early 2000's than initially anticipated. OSA anticipates this could roughly double the Retroactive costs from their previous estimates
  - When combined with the impact of bullet 1, above, OSA believes the overall Retroactive costs could be around 50 percent larger than what is shown in the table above

## OTHER STATES

LEOFF Plan 2 contacted staff from other state retirement systems for information and data regarding their members' receipt of interruptive military service credit, as well as the requirements for receiving such credit.

Idaho PERS allows their members a maximum of five years of no-cost military service credit, similar to Washington. Wisconsin Retirement Systems allows a maximum of four years of no-cost military service credit, unless the service is involuntary. Minnesota Retirement Systems and Oregon PERS do not offer no-cost interruptive military service credit. Research and communications with staff members from other state retirement systems shows that none of these states require their members to have earned a specific medal, or to have served in a specific conflict to receive no-cost or partially subsidized interruptive military service credit. Among the states that provided information and offer no-cost interruptive military service credit, the requirements for earning no-cost credit are much broader than Washington.

Below is a comparison among other states based on total members, members receiving interruptive military service credit, average no-cost service credit received, maximum amount of no-cost service granted, and qualifications to receive no-cost military service credit.

| STATE                | TOTAL MEMBERS | MEMBERS WITH INTERRUPTIVE MILITARY SERVICE CREDIT | AVERAGE SERVICE CREDIT RECEIVED | MAXIMUM NO-COST SERVICE CREDIT GRANTED | QUALIFICATIONS FOR NO-COST SERVICE CREDIT  |
|----------------------|---------------|---|---------------------------------|--|--|
| IDAHO (PERSI)        | 160,000       | 500   | 5-6 months                      | 5 years                                | Member must enter military service within 90 days of leaving PERSI employment, and must return to PERSI employment within 90 day of release from active duty.              |
| MINNESOTA (MSRS)     | 134,000       | 12  | –                               | n/a                                    | No-cost credit not offered.  |
| OREGON (PERS)        | 374,000       | 1,083   | –                               | n/a                                    | No-cost credit not offered. Must be purchased by member or employer.   |
| WASHINGTON (DRS)     | 523,000       | 8,339   | 9 months                        | 5 years                                | Must have been awarded a campaign medal from serving in combat zones.  |
| WASHINGTON (LEOFF 2) | 24,000        | 574   | 10 months                       | 5 years                                | Must have been awarded a campaign medal from serving in combat zones.  |
| WISCONSIN (WRS)      | 642,000       | 784   | 2 years                         | 4 years                                | Left WRS employment to serve in the armed forces and return to employment within 180 days. Member may be responsible for employee contributions, under some circumstances. |

## SUPPORTING INFORMATION

**Appendix A:** September 2021 Letter from the Office of the State Actuary regarding Interruptive Military Service Credit



# Office of the State Actuary

*“Supporting financial security for generations.”*

September 16, 2021

Jacob White  
Senior Research & Policy Manager  
LEOFF Plan 2 Retirement Board

*Delivered via email.*

## **SUBJECT: UPDATE ON IMSC FOR EXPEDITIONARY MEDALS**

As requested, this letter shares the estimated cost of providing Interruptive Military Service Credit (IMSC) for members of the Law Enforcement Officers’ and Fire Fighters’ Retirement Plan 2 (LEOFF 2) who have earned an Expeditionary Medal. It’s our understanding that this communication is intended to provide Board members with a general sense for the expected costs when evaluating their policy options.

More specifically, the contribution rate and budget impacts table matches our analysis from the 2020 Interim [IMSC Study](#) for the Select Committee on Pension Policy (SCPP), pages 74-81. We also wanted to illustrate how these pricing results may change given the new data from the Department of Defense (DoD) that was received late last year.

In terms of next steps, we will incorporate any feedback from the Board and prepare updated pricing analysis for your November meeting. Otherwise, please let us know if you have any questions or how we can be of any further assistance.

Best Regards,

Michael T. Harbour, ASA, MAAA  
Actuary

### Summary of Analysis

cc: Steve Nelsen,  
Executive Director, LEOFF Plan 2 Retirement Board  
Lisa A. Won, ASA, FCA, MAAA  
Deputy State Actuary, Office of the State Actuary  
Kyle Stineman, ASA, MAAA  
Actuary, Office of the State Actuary

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## SUMMARY OF ANALYSIS

The following tables show the prior pricing results of providing IMSC for members of LEOFF 2 who earn an Expeditionary Medal (1) in the future, and (2) in the past. Please see our IMSC Study (starting on page 74) for the data, assumptions, and methods used to prepare this analysis, as well as some commentary on risk as it relates to this proposal.

| <b>(1) Prospective</b>              |         |
|-------------------------------------|---------|
| <b>Impact on Contribution Rates</b> |         |
| System/Plan                         | LEOFF 2 |
| Current Members                     |         |
| Employee                            | 0.0013% |
| Employer                            | 0.0008% |
| State                               | 0.0005% |

| <b>25-Year Budget Impacts</b> |              |
|-------------------------------|--------------|
| (Dollars in Millions)         | LEOFF 2      |
| 2021-2046                     |              |
| General Fund                  | \$0.3        |
| Non-General Fund              | 0.0          |
| <b>Total State</b>            | <b>\$0.3</b> |
| Local Government              | 0.4          |
| <b>Total Employer</b>         | <b>\$0.7</b> |
| <b>Total Employee</b>         | <b>\$0.7</b> |

*Note: Totals may not agree due to rounding.*

| <b>(2) Retroactive</b>              |         |
|-------------------------------------|---------|
| <b>Impact on Contribution Rates</b> |         |
| System/Plan                         | LEOFF 2 |
| Current Members                     |         |
| Employee                            | 0.019%  |
| Employer                            | 0.012%  |
| State                               | 0.008%  |

| <b>25-Year Budget Impacts</b> |            |
|-------------------------------|------------|
| (Dollars in Millions)         | LEOFF 2    |
| 2021-2046                     |            |
| General Fund                  | \$4        |
| Non-General Fund              | 0          |
| <b>Total State</b>            | <b>\$4</b> |
| Local Government              | 5          |
| <b>Total Employer</b>         | <b>\$9</b> |
| <b>Total Employee</b>         | <b>\$9</b> |

*Note: Totals may not agree due to rounding.*

As discussed in the IMSC Study (page 80), we received additional data from the DoD after completing our original analysis. Based upon this new info, we share the following:

- A. The ratio of Expeditionary-to-Campaign Medals could be lower than our assumed one-to-one relationship, thus potentially reducing the expected cost of this proposal by approximately 25 percent – both Prospective and Retroactive.
- B. At the same time, it appears that Expeditionary Medals were granted at a higher rate in the early 2000's than initially anticipated. By itself, we anticipate this could roughly double the Retroactive costs from our previous estimates.
  - When combined with the impact of bullet A, above, we believe the overall Retroactive costs could be around 50 percent larger than what is shown in the table above.



### ***Actuarial Disclosures***

We believe the information presented in this letter is reasonable for the primary purpose stated on page 1; continued reliance on these results beyond the September meeting may not be appropriate. Specifically, we caution that updated analysis could be impacted by the results of our [2020 Actuarial Valuation Report](#) (AVR), as well as possible changes from the state actuary's recommendations as part of the [2021 Report on Financial Condition and Economic Experience Study](#). Lastly, please see the "Comments on Valuation Model" section within our 2020 AVR for new required actuarial disclosures that are applicable to the same software used to prepare the historical pricing results.

The Office of the State Actuary ("we") prepared this analysis and provided opinions in accordance with Washington State law and accepted Actuarial Standards of Practice. Michael T. Harbour meets the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein. While this communication is meant to be complete, we are available to provide extra advice and explanations as needed.



# Interruptive Military Service Credit

Comprehensive Follow-up Report  
September 29, 2021

# Issue

- **Should eligibility for no-cost interruptive military service credit be expanded from those who earned campaign medals to also include those who earned expeditionary medals?**



# LEOFF 2 Board 2020 Recommendation

- In 2020 the Legislature required the LEOFF 2 Board and the SCPP to submit studies with recommendations on whether to expand eligibility for no-cost interruptive military service credit
- The Board voted to defer until next year making a recommendation to expand the no-cost interruptive military service credit benefit to service where the member earned an expeditionary medal
  - The Board expressed support of the policy to expand
  - The Board also expressed concerns regarding the cost of the benefit and the expected state and local budget environment due to revenue impacts from Covid-19

# Background

- A member qualifies for this benefit when they take a leave of absence from a DRS covered position to serve in the United States military and the member returns to their employer after their military service is complete
- Two types:
  - Fully subsidized (no-cost interruptive military service credit)
  - Partially subsidized (reduced-cost interruptive military service credit)

# Eligibility

- To receive no-cost service credit, a DRS member must meet the definition of “veteran” under RCW 41.04.005 meaning the member:
  - Served during World War I, World War II, the Korean conflict, the Vietnam era, the Persian Gulf War, and any future period of war declared by Congress, or
  - Earned a campaign badge or medal

# Legislative History

- **2020**

- HB 2544 redefined “period of war” to no longer identify specific conflicts and instead recognize all service from which a campaign badge or medal was earned
- HB 2544 initially proposed amending RCW 41.04.005 to expand the definition of “period of war” to include those who received an expeditionary medal
- The unknown cost of including to expeditionary medals resulted in an amendment requiring LEOFF 2 and the SCPP to study this expansion of no-cost service credit eligibility

- **2021**

- The Board and the SCPP submitted their studies, and there were no bills to expand eligibility

# Department of Defense Categories of Medals

- **Campaign Medal**
  - Recognize the highest level of personal risk and hardship for members who are deployed to the geographic areas where the combat is actually occurring
- **Expeditionary Medal**
  - Recognize high levels of personal risk and hardship for members deployed in support of combat operations, but who are not in the geographic area where the actual combat is occurring

# Proposed Expansion of Eligibility

- Expand eligibility to interruptive service where an Expeditionary Medal was earned
- Members who purchased partially subsidized service credit and whose service meets the new eligibility requirements would receive a refund for that payment
- Retirees whose service meets the new eligibility requirements would have their benefit recalculated prospectively only

# Example 1 – Retiree purchased service credit

- A retired law enforcement officer earned an expeditionary medal during interruptive military service from their DRS covered position. When retiring they choose to purchase partially subsidized service credit for this interruptive service
- Under the proposal, this retiree would receive a refund from DRS for the payment they made to purchase the partially subsidized service credit and they would continue to receive the same monthly pension payment

## Example 2 – Retiree did not purchase service credit

- A retired fire fighter earned an expeditionary medal during interruptive military service from their DRS covered position. When retiring they choose not to purchase partially subsidized service credit for this interruptive service.
- Under the proposal, this member would have their benefit recalculated prospectively to include the additional no-cost interruptive military service credit they are now eligible for
- This member would not receive a retroactive payment adjusting their benefit from their retirement date



# 2020 Actuarial Fiscal Note

| <b>(1) Prospective</b>              |                |
|-------------------------------------|----------------|
| <b>Impact on Contribution Rates</b> |                |
| <b>System/Plan</b>                  | <b>LEOFF 2</b> |
| <b>Current Members</b>              |                |
| Employee                            | 0.0013%        |
| Employer                            | 0.0008%        |
| State                               | 0.0005%        |

| <b>25-Year Budget Impacts</b> |                |
|-------------------------------|----------------|
| <i>(Dollars in Millions)</i>  | <b>LEOFF 2</b> |
| <b>2021-2046</b>              |                |
| General Fund                  | \$0.3          |
| Non-General Fund              | 0.0            |
| <b>Total State</b>            | <b>\$0.3</b>   |
| Local Government              | 0.4            |
| <b>Total Employer</b>         | <b>\$0.7</b>   |
| <b>Total Employee</b>         | <b>\$0.7</b>   |

*Note: Totals may not agree due to rounding.*

| <b>(2) Retroactive</b>              |                |
|-------------------------------------|----------------|
| <b>Impact on Contribution Rates</b> |                |
| <b>System/Plan</b>                  | <b>LEOFF 2</b> |
| <b>Current Members</b>              |                |
| Employee                            | 0.019%         |
| Employer                            | 0.012%         |
| State                               | 0.008%         |

| <b>25-Year Budget Impacts</b> |                |
|-------------------------------|----------------|
| <i>(Dollars in Millions)</i>  | <b>LEOFF 2</b> |
| <b>2021-2046</b>              |                |
| General Fund                  | \$4            |
| Non-General Fund              | 0              |
| <b>Total State</b>            | <b>\$4</b>     |
| Local Government              | 5              |
| <b>Total Employer</b>         | <b>\$9</b>     |
| <b>Total Employee</b>         | <b>\$9</b>     |

*Note: Totals may not agree due to rounding.*

# 2021 Actuarial Fiscal Note

LEOFF 2 Board received a response to a FOIA request from the Department of Defense last December, OSA reviewed this data and provided the Board with their initial analysis

1. The ratio of Expeditionary-to-Campaign Medals could be lower than previously expected, potentially reducing the expected cost of this proposal by approximately 25 percent – both Prospective and Retroactive
2. At the same time, it appears that Expeditionary Medals were granted at a higher rate in the early 2000's than initially anticipated. OSA anticipates this could roughly double the Retroactive costs from their previous estimates
  - When combined with the impact of bullet 1, above, OSA believes the overall Retroactive costs could be around 50 percent larger than what is shown in the previous table

# SCPP

- In 2020, the SCPP also voted to defer recommending expanding the no-cost interruptive military service credit benefit to service where the member earned an expeditionary medals until next year
- SCPP is planning on scheduling an initial briefing in October from SCPP staff
- SCPP staff is coordinating with LEOFF 2 Board staff

# Next Steps

- LEOFF 2 Board will receive a final briefing on this issue in November



**Thank You**

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# Benefit Improvement Account 4<sup>th</sup> Educational Briefing

September 29, 2021

# Previous BIA Educational Briefings

1. Benefit improvement proposed as part of SB 5453, including OSA presentation on their fiscal note
2. The mechanics and impact of using the LEOFF 2 Benefit Improvement Account to pay for a benefit improvement; issues related to purchase with BIA when the BIA does not have enough money to fully pay for the benefit
3. The Board's policy goals of purchasing a benefit improvement using the BIA

# Purpose of Today's Briefing

- Number of questions came up during previous BIA briefings
- Review these questions and provide an opportunity for input from the Board to determine next steps



# Active Member Benefit Questions

1. Should the demarcation date between qualifying for the lump sum vs qualifying for the increased multiplier be back-dated prior to the passage of a bill or after the effective date of the bill?
2. Should members who retire after the passage of the bill, with less than 15 years of service, receive a lump sum payment?

# Retired Member Benefit Questions

1. Should retirees have an option to purchase an annuity with their lump sum payment?
2. Should the lump sum payment go to all employees regardless of years of service?

# Funding Questions

1. Does the Board want to receive options from OSA on the potential issues regarding the intent of the BIA to pre-fund a benefit and the Board's current funding policy?

# Next Steps

- Is there consensus on how the Board would like to address any of the issues discussed today?
- If not, does the Board want staff to bring back additional information (i.e. detailed pros and cons) of the remaining questions for November meeting?



**Thank You**

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# Survivor Option Reelection

2<sup>nd</sup> Follow-up  
September 29, 2021

# Issue

**Allowing members to change their survivor option election after retirement may raise plan qualification issues with the IRS**

# Legislative Background

**The LEOFF 2 Board endorsed legislation to allow LEOFF 2 retirees up to 90 calendar days after the receipt of their first retirement allowance to prospectively change their survivor election**

- **The bill was amended to include all DRS covered retirement plans**

**Tax counsel identified possible plan qualification issues with the bill**

- **The bill was amended to not take effect until the state received determination from the IRS that these changes conform to federal law**
- **The amended bill passed and was signed into law**



# Request for Private Letter Ruling

- DRS, in consultation with the LEOFF 2 Board, requested Private Letter Ruling from IRS
- Tax Counsel drafted and submitted the request for a Private Letter Ruling
- Request was for one Private Letter Ruling for all DRS systems/plans
- Request filed in February 2021

# Update from Tax Counsel

- **IRS ruled that SB 6417 conforms with federal law**
  - **“the minimum distribution requirements of § 401(a)(9) are not violated due to [SB 6417], which allows current and future participants in the plans administered by [DRS] to change their survivorship benefit election within 90 days after receipt of their first retirement allowance.”**

# DRS Next Steps

- DRS is coordinating with LEOFF 2 staff on implementation of the law
- DRS project team is currently defining a permanent process and system updates
- DRS priority is to focus on WAC updates first
- Initial decisions DRS made in terms of processing:
  - Law is effective August 3, 2021
  - 90 day window will begin when DRS issues payment, this is typically the last business day of the month
  - Members who retired prior to the effective date may still be able to change their survivor option if it has been less than 90 days since they received their first pension payment
  - Limit to one change during the 90 day window



**Thank You**

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