BOARD MEETING AGENDA

NOVEMBER 17, 2021 • 9:30AM

LEOFF Plan 2 Retirement Board

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.**

1.	**Approval of Minutes**	**9:30 AM**
2.	**WSIB Annual Update** *Theresa Whitmarsh, Executive Director*	**9:35 AM**
3.	**Tiered Multiplier Benefit Improvement** (Comprehensive) *Jacob White, Sr. Research and Policy Manager*	**10:05 AM**
4.	**Interruptive Military** (Final) *Jacob White, Sr. Research and Policy Manager*	**10:40 AM**
5.	**2020 Actuarial Valuation Results** *Mitch DeCamp, Senior Actuarial Analyst, OSA*	**11:05 AM**
6.	**Roth Deferred Option** (Comprehensive) *Jacob White, Sr. Research and Policy Manager*	**11:35 AM**
7.	**Administrative Update**	**12:00 PM**
8.	**Economic Assumption Adoption** *Steve Nelsen, Executive Director*	**12:15 PM**
9.	**2022 Meeting Calendar Adoption**	**12:45 PM**

**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.

WASHINGTON STATE INVESTMENT BOARD: ANNUAL UPDATE – 2021

LEOFF 2 BOARD

NOVEMBER 17, 2021

Theresa Whitmarsh

Chief Executive Officer

OVERVIEW OF THE WSIB

Asset Management Profile

- $186.3 billion in assets under management as of September 30, 2021
- 17 pension funds
- 5 Labor and Industry Funds
- 16 permanent and other trust funds

Mission

- Maximize investment returns at a prudent level of risk in order to meet the financial objectives of those we serve

Investment scope and scale

- 76 different countries
- Across 6 continents and 49 currencies
- More than 14,000 investment holdings

- Board comprised of 15 members
  - 10 voting members
  - Advised by 5 non-voting investment professionals, who are selected by the voting Board members

3 EX-OFFICIO MEMBERS			2 LEGISLATORS	
Mike Pellicciotti	Tracy Guerin	Joel Sacks	Timm Ormsby	Mark Mullet
The State Treasurer	Director of DRS (Chair)	Director of L&I	Member of the House of Representatives	Member of the Senate
5 REPRESENTATIVES OF THE PUBLIC EMPLOYEE PENSION SYSTEMS				
Greg Markley	Judy Kuschel	Yona Makowski	Sara Ketelsen	Vacant
Member of LEOFF (Vice-Chair)	Active Member of PERS	Retired Member of State Pension System	Member of TRS	Member of SERS
INVESTMENT PROFESSIONALS				
David Nierenberg	William A. Longbrake	Ada Healey	Mary Pugh	George Zinn

WHO WE ARE – STAFFING AND INVESTMENT PARTNERS

- **Staffing: 115 employees**
- **Two offices: Olympia and Seattle; remote work since March 2020**
- **130+ external investment managers and partners across five asset classes**
- **60 investment professionals**
- **55 financial/accounting professionals and executive/administrative staff**
- **Mission-driven culture based on non-negotiable integrity and fiduciary duty**

WSIB INVESTMENT RESPONSIBILITY (38 FUNDS MANAGED)

17 Retirement Funds

- Public Employees' Plans 1, 2, 3
- School Employees' Plans 2, 3
- Teachers' Plans 1, 2, 3
- Law Enforcement Officers' and Firefighters' Plans 1, 2
- Judicial Retirement Account – Defined Contribution
- Washington State Patrol Plans 1, 2
- Volunteer Firefighters' and Reserve Officers' Relief and Pension
- Deferred Compensation Program
- Public Service Employees' Plan 2
- Higher Education Retirement Plan Supplemental Benefit

Labor & Industries' Funds 7

- Accident
- Medical Aid
- Pension Reserve
- Supplemental Pension
- Industrial Insurance Rainy Day (unfunded)

5 Permanent Funds

- Agricultural College
- Common School
- Normal School
- Scientific
- State University
- American Indian Endowed Scholarship
- Foster Care Endowed Scholarship (unfunded)

Other Funds 9

- Guaranteed Education Tuition
- Developmental Disabilities Endowment (Private and State)
- Washington State Opportunity Scholarship (Scholarship, Endowment, Tech Pathway, and Degree Pathway)
- Long-term Services and Support (unfunded)
- Dan Thompson Memorial

RETIREMENT PLANS AND MARKET VALUES

SEPTEMBER 30, 2021

- **DB plans and hybrid DB/DC plans commingled into one investment fund (CTF) run by the WSIB**

Defined Benefit and Hybrid Defined Benefit/Defined Contribution Plans	Market Value
Public Employees' Retirement System Plan 1 (PERS)	$9,398,513,425
Public Employees' Retirement System Plan 2/3	$61,095,868,890
Teachers' Retirement System Plan 1 (TRS)	$7,008,777,066
Teachers' Retirement System Plan 2/3	$30,281,792,018
Washington State Patrol Retirement System Plan 1 (WSPRS)	$1,574,250,382
Washington State Patrol Retirement System Plan 2	$174,752,857
Law Enforcement Officers' & Fire Fighters' Plan 1 (LEOFF)	$7,201,364,138
Law Enforcement Officers' & Fire Fighters' Plan 2	$19,489,154,965
School Employees' Retirement System Plan 2/3 (SERS)	$10,575,458,521
Public Safety Employees' Retirement System Plan 2 (PSERS)	$1,204,208,046
Higher Education Supplemental Insurance Plan	$153,904,646
Total	$148,158,044,956

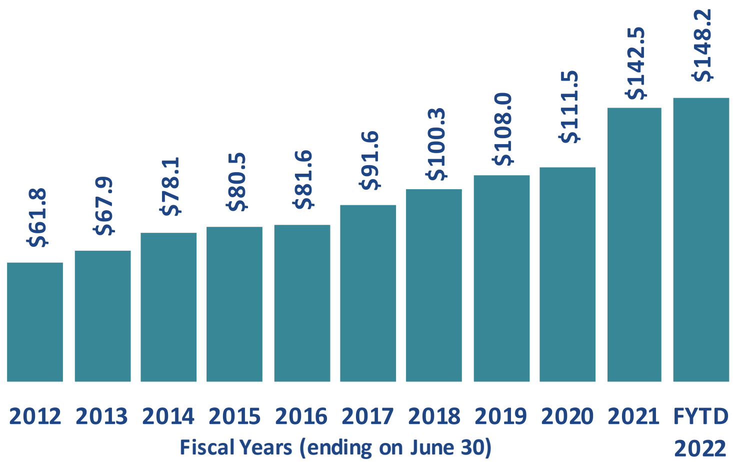
Retirement Plan(s) Outside the CTF	Market Value
Volunteer Fire Fighters' and Relief Officers' Pension Fund (VFFRO)	$251,500,402
Total	$251,500,402

Defined Contribution Plans	Market Value
Plans 3 Outside of the CTF	$7,214,019,240
Deferred Compensation Program (DCP)	$6,135,143,043
Judicial Retirement Account (JRA)	$9,441,439
Total	$13,358,603,721

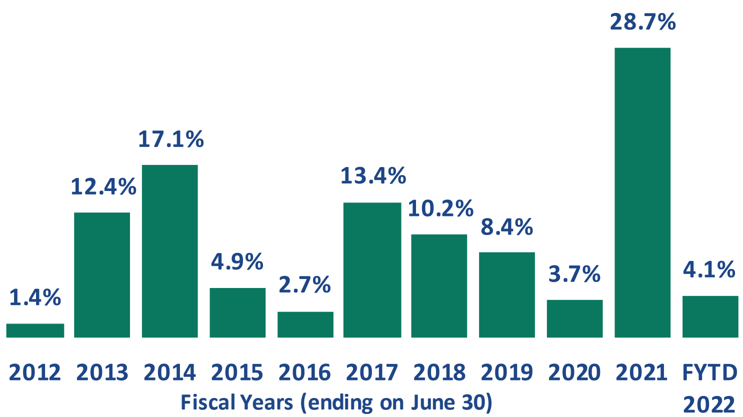
COMMINGLED TRUST FUND MARKET VALUES AND PERFORMANCE

SEPTEMBER 30, 2021

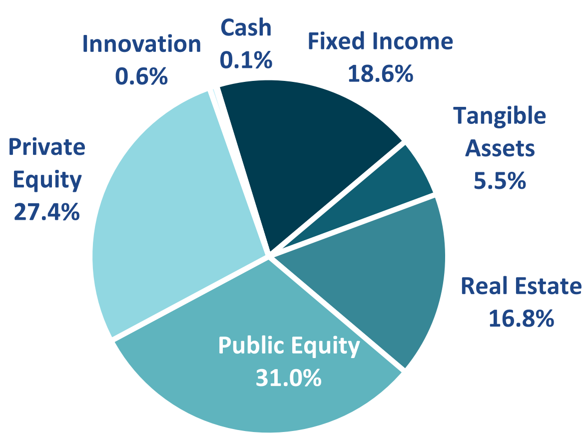
Historical Market Value ($ Billions)



Historical Annual (FY) Returns



Asset Allocation



Market Values and Returns

	(000s)	1 Year	3 Year	5 Year	10 Year	20 Year
Total CTF	$148,158,044,955	26.9%	13.7%	12.7%	11.2%	8.9%
Fixed Income	$24,722,791,820	0.2%	6.5%	4.1%	4.0%	5.2%
Tangible Assets	$8,136,341,687	16.4%	6.4%	6.8%	5.1%	N/A
Real Estate	$24,946,970,381	16.8%	22.1%	13.7%	12.4%	12.5%
Public Equity	$46,396,593,482	29.5%	12.5%	13.4%	12.5%	8.5%
Private Equity	$40,638,549,774	55.8%	22.7%	20.7%	16.2%	12.8%
Innovation	$844,711,498	26.9%	14.5%	-5.2%	2.8%	N/A
Cash	$2,472,086,311	0.1%	1.2%	1.3%	0.7%	1.4%

WHAT WE DO – MARKET RISK SPECTRUM

- WSIB seeks diversification across the portfolio and within each asset class
- Implementation within each asset class will determine how risk is concentrated
- Weight of each asset class must match risk profile

Lower Risk ——— **Higher Risk**

FIXED INCOME

Treasury Bills · Credit Bonds · High Yield

TANGIBLE ASSETS

Less Leverage
Income Producing
Fully Hedged

Levered
Speculative Construction
Unhedged

REAL ESTATE

Less Leverage
Developed Markets
Fully Developed

Levered
Emerging Markets
Raw Land

PUBLIC EQUITY

Developed Markets
Large Cap

Emerging Markets
Small Cap

PRIVATE EQUITY

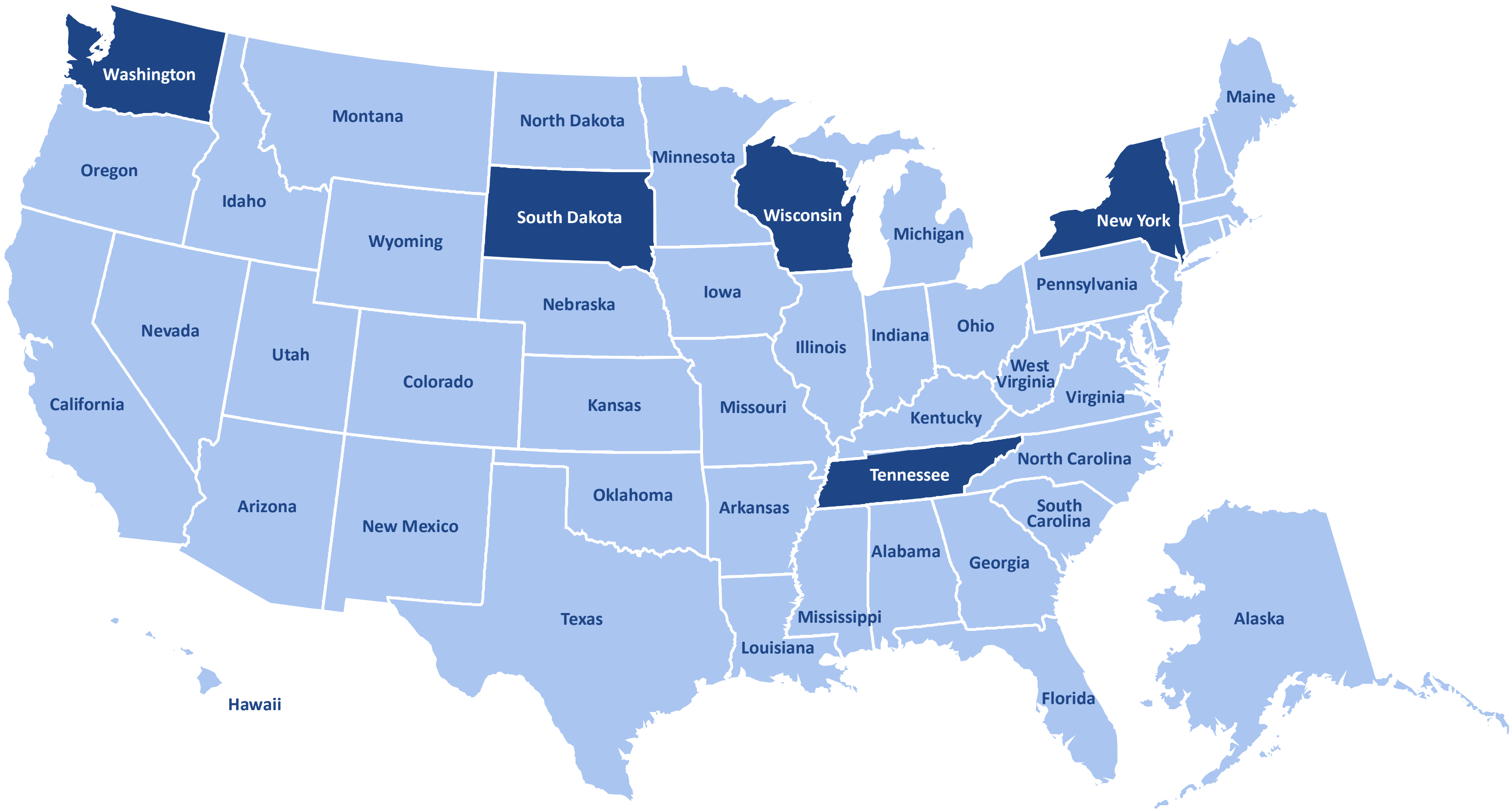
Mezzanine Debt · Large Buyouts · Venture Capital

Representative Only, Not to Scale

OUR RESULTS – A STRONG REPUTATION

ONE OF THE BEST FUNDED PENSION SYSTEMS IN THE NATION

Top 5 Funded States



Source: The PEW Charitable Trusts, Fiscal Year 2019

KEY INITIATIVES

Leadership transition moving forward

- Allyson Tucker confirmed as new CEO, starts January
- Curt Gavigan on board as Chief Operating Officer
- Actively recruiting for future CIO

TAP into TDF launched in October for Plan 3 and Deferred Comp Plan

- Extends full diversification (private markets) into Target Date Funds
- Enhances risk-adjusted returns within the age-adjusted fund glidepath
- Strong collaboration between WSIB and DRS team

Developing investment plan for new WA Cares program

- Dedicated portfolio with a fixed income investment plan
- Goal is to create the most advantageous investment program permitted under law
- Management of assets to begin during 2Q 2022

Launched new Diversity, Equity and Inclusion Committee

- Robust participation and engagement among staff
- Catalyst for surfacing vital management and culture issues

IN SUMMARY

Fulfillment of mission and fiduciary duty will remain front and center

Focus on retaining and attracting top talent will be a continued focus

Resources will be managed to support retirement plans plus a broader array of vital stakeholder interests

Management of ESG factors (e.g., climate, diversity) must be integrated effectively into investment process and strategies

Reshaped global economy will require mix of adaptation and unwavering discipline

LEOFF Plan 2 Retirement Board

November 17, 2021

Tiered Multiplier Benefit Improvement

COMPREHENSIVE REPORT

By Jacob White

Senior Research & Policy Manager

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ISSUE STATEMENT

A benefit improvement purchased using the Benefit Improvement Account should meet the policy goals of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Board while also adhering to the legislative intent of the Benefit Improvement Account.

OVERVIEW

This report will provide background on the history and purpose of the LEOFF Plan 2 Benefit Improvement Account (BIA). It will also identify policy options for the Board to consider with purchasing a benefit improvement using the BIA.

BACKGROUND AND POLICY ISSUES

History of the Benefit Improvement Account

In 2008, the legislature created the Benefit Improvement Account (BIA). The BIA was initially to be funded through periodic appropriations from the State's General Fund when certain revenue criteria were met. Despite those criteria being met, the appropriations were never made and instead, the BIA has been funded through transfers from the LEOFF Plan 2 Trust Fund into the BIA.

In creating the BIA the legislature recognized that:

> the current benefit formula and contributions for [LEOFF] 2 are inadequate to modify that formula in recognition of the shorter working careers for firefighters and police officers. […] In recognition of the physical demands of the professions and the inherent risks faced by law enforcement officers and firefighters, eligibility for retirement in [LEOFF] 2 system has been set at age fifty-three. However, the benefit formula is designed for careers of thirty-five to forty years, making retirement at age fifty-three an unrealistic option for many.[1]

[1] https://lawfilesext.leg.wa.gov/biennium/2007-08/Pdf/Bills/Session%20Laws/Senate/6573-S.SL.pdf?cite=2008%20c%2099%20%C2%A7%203

The minimum amount of income often cited as necessary for income replacement at retirement is 60%. The benefit formula for the Department of Retirement Systems (DRS) administered pension systems, including LEOFF Plan 2, is: 2% x Years of Service x Final Average Salary. To reach 60% replacement income using this formula a member must have a 30-year career.

In the state pension systems for general public employees, teachers, school employees, and most other public employees in Washington State, the normal retirement age is 65 years old. However, for LEOFF Plan 2 normal retirement age is 53 years old.[2] The earlier normal retirement age is due to the physical demands and risks inherent in LEOFF covered positions. This, coupled with a benefit formula designed for 30-year careers, results in the average LEOFF Plan 2 member replacing only approximately 47% of their pre-retirement income through their LEOFF Plan 2 benefit. The 2020 projected average salary of a LEOFF 2 member is $10,390 per month. The average LEOFF Plan 2 member retires at age 56 with 23.5 years of service. These averages would result in a benefit of $4,883 per month.

Policy Goals of the Board

One policy goal frequently discussed by the Board is that this benefit improvement should apply as broadly as possible. The Board has discussed providing a benefit to as many members as possible while also recognizing the limitations of the cost of the benefit. The Board recognized that the BIA was funded by transfers from the LEOFF Plan 2 trust fund, which contains contributions made by active and retired LEOFF Plan 2 members. Therefore, the Board reasoned that current members and retirees should receive a benefit since they have already helped pay for it through past contributions. Furthermore, the Board discussed prioritizing a larger benefit for members who spend a career in LEOFF Plan 2, since the longer someone worked in a LEOFF 2 covered position the larger their contribution to the funds in the BIA.

The Board has also discussed a policy goal to improve retention with the benefit improvement. One of the primary goals of any pension plan is to recruit and retain employees. Employers may be particularly interested in improving recruitment and retention through the benefit improvement.

Lump Sum Benefit

The Board has identified a lump sum benefit as a benefit improvement option for LEOFF Plan 2 retirees. A lump sum benefit is a one-time payment made to retirees from the BIA. The issue

[2] Normal Retirement age for Public Safety Employees' Retirement System (PSERS) Plan 2 is 62, and LEOFF 1 is 50

the Board has identified with a lump-sum benefit is how to design that benefit in a way that best meets the Board's policy goal of equity.

The options identified by the Board are:
1. $20,000 lump sum for retirees; or
2. $100 per month of service credit for retirees.

Option 1 would be less complex to administer. It provides the same benefit to all vested members, which may be viewed as the most straightforward way to distribute a benefit. However, from an accumulated contributions standpoint, it may be considered unfair for a member with 5 years of service credit to receive the same benefit as a member with 20 or more years.

Option 2 addresses this issue of proportionality by providing a lump sum benefit based on the amount of service credit a retiree has earned. For example, a retiree with 5 years of service credit (60 months of service credit) would receive a lump sum payment of $6,000; a retiree with 10 years of service credit (120 months of service credit) would receive a lump sum payment of $12,000; a retiree with 20 years of service (240 months of service credit) would receive a lump sum payment of $24,000; and, a retiree with 25 years of service (300 months of service credit) would receive a lump sum payment of $30,000.

This option would also provide a minimum benefit of $20,000 to catastrophic or duty disability retirees, as well as duty death beneficiaries. While Option 2 would be more complex to administer, it provides a benefit that meets the Board's goal of providing more benefit to career employees.

The Board has also discussed providing retirees who receive a lump sum benefit the option of purchasing an actuarially equivalent annuity with those funds. This is a benefit that can be provided at no-cost to the plan. However, there is some risk in allowing members to purchase an annuity, as the experience of the plan could result in not aligning with the assumptions used by the Office of the State Actuary (OSA) in pricing the annuity factors for purchasing an annuity. Although, there is the possibility that the experience of the plan could result in a savings. This is a risk that the plan already takes on with the Purchase of Additional Annuity and Purchase of Service Credit benefits.

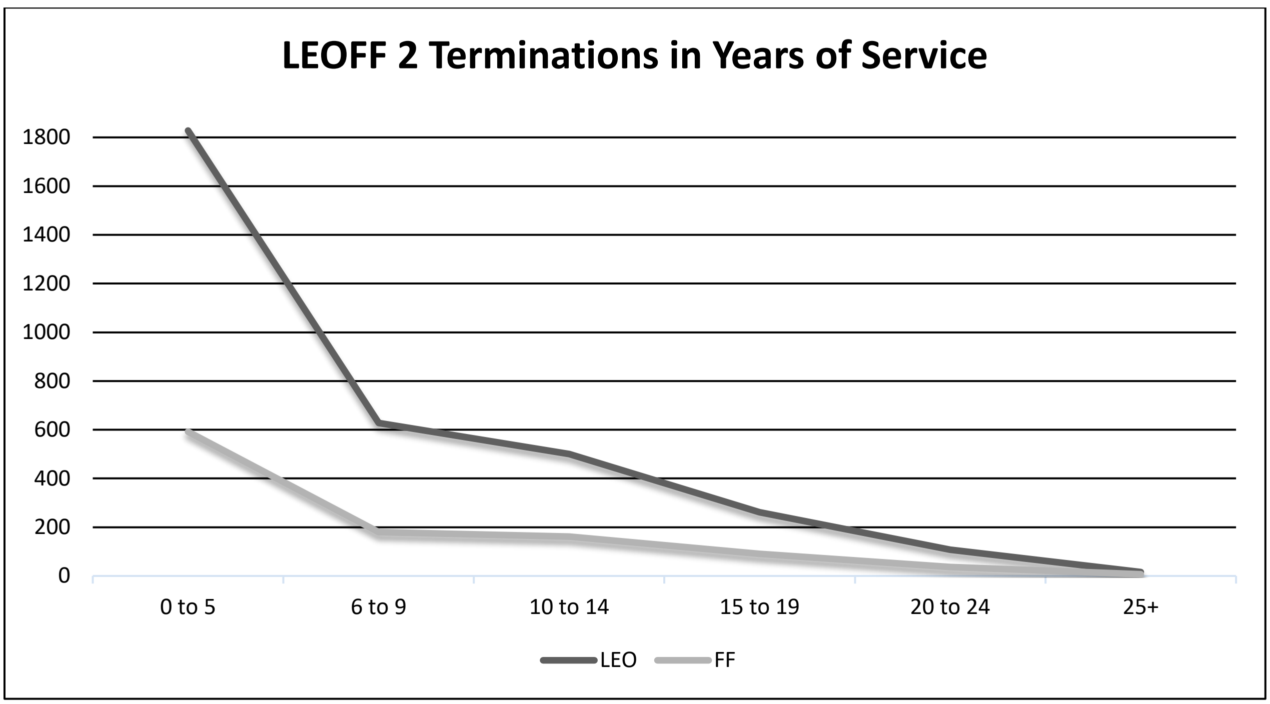
Tiered Multiplier Benefit

The Board has identified a tiered multiplier as a benefit improvement for active members that meets its policy goals of equity and retention. The tiered multiplier benefit would increase the plan benefit multiplier from 2% to 2.5% for the years of service between 15 and up to 26.

This benefit would improve retirement income so that retirees can be closer to the 60% income replacement goal, while also incentivizing members to remain in LEOFF Plan 2. OSA estimated that the average member's retirement benefit will increase by about 9 percent with a mid-career multiplier.[3]

The years of service between 15 and 26 were identified in part because, by this point, employers have significantly invested in their employees' training and employees have greater knowledge through their extensive work experience. However, a concern with this benefit improvement is that it does not provide a benefit to members who work less than 15 years. The Board has recognized that this concern could be addressed by providing the lump sum benefit to members who work less than 15 years.

Below is a chart of data from 1995-2015 that shows at what service credit range fire fighters and law enforcement officers terminated from LEOFF service:



Who qualifies for which benefit improvement?

Determining who qualifies for which benefit improvement is driven by the policy goals of the Board discussed above. In particular, the Board recognizes that the BIA was funded by transfers from the LEOFF Plan 2 trust fund, which contains contributions made by active and retired LEOFF Plan 2 members.

[3] https://fnspublic.ofm.wa.gov/FNSPublicSearch/GetPDF?packageID=62887

Also, since there are different benefits for retirees versus active members versus new hires, the Board has discussed the importance of identifying a date in the bill which determines the benefit a person will qualify for. The Board has also discussed backdating that delineation date in the bill so that it does not cause unexpected issues for the plan, such as a surge in retirements or members delaying planned retirement. The date that has been identified for delineating these benefits is February 1, 2021.

Below is a table breaking down which groups of LEOFF Plan 2 members qualify for the lump sum benefit improvement, tiered multiplier benefit improvement, choice between lump sum benefit or tiered multiplier benefit, or no benefit improvement. This list does not specify all potential situations.

Retired as of 2/1/21	
LEOFF 2 Member Group	**Benefit Improvement**
Retired as of 2/1/21	Lump sum
Duty or catastrophic disability retired as of 2/1/21	Lump sum (minimum of $20k)
Beneficiary of line-of-duty death who died prior to 2/1/21	Lump sum (minimum of $20k)
Survivor beneficiary, member deceased as of 2/1/21	Lump sum
Member deceased as of 2/1/21 with no survivor beneficiary	No benefit
Withdrawn	No benefit

LEOFF 2 Member Active as of 2/1/21	
LEOFF 2 Member Group	**Benefit Improvement**
Still active	Choice of lump sum or tiered multiplier
Now retired	Choice of lump sum or tiered multiplier
Duty or catastrophic disability retirement	Choice of lump sum (minimum of $20k) or tiered multiplier
Beneficiary of line-of-duty death who was active as of 2/1/21	Choice of lump sum (minimum of $20k) or tiered multiplier
Survivor beneficiary, member deceased after 2/1/21	Choice between a lump sum or tiered multiplier benefit at retirement
Survivor beneficiary in service death not line-of-duty	Choice of lump sum or tiered multiplier
No survivor beneficiary, member deceased after 2/1/21 before effective date of the bill	Lump sum to beneficiary or estate
No survivor beneficiary in service death not line of duty	Lump sum to beneficiary or estate
Withdrawn	No benefit
Inactive as of 2/1/21 and vested	Choice of lump sum or tiered multiplier
Inactive and not vested	No benefit
Inactive and not vested as of 2/1/21, returns to LEOFF employment after 2/1/21 and becomes vested	Choice of lump sum or tiered multiplier

New Member after 2/1/21	
LEOFF 2 Member Group	**Benefit Improvement**
New members after 2/1/21	Tiered multiplier
Withdrawn	No benefit

Members active as of February 1, 2021 would receive the option of choosing between the lump sum benefit or the tiered multiplier. Some of the policy reasons for this choice are that these members contributed to the funds used to purchase the benefit improvement and may be at a point of their career where the tiered multiplier could help their employer retain them. The following is an example of how this choice of benefit would work for this group of members:

> Member is currently 45 years old with 20 years of service credit. They work for an additional 10 years and retire at age 55 with an Average Final Compensation of $10,000. This member will have two benefit options at retirement:
>
> - Option 1: 2% x 30 yrs x $10k for a monthly benefit of $6000 plus a lump sum of $36,000
> - Option 2: (2% x 20 yrs + 2.5% x 10 yrs) x $10K for a monthly benefit of $6500

This option would also apply to members who are inactive as of February 1, 2021 but not retired. Some of the policy reasons behind offering these members the option between the benefits are that they also have contributed to the benefit improvement account and offering them the potential incentive of the tiered multiplier may bring them back to LEOFF service. The following is an example of how this choice of benefit would work for this group of members:

> Member is currently inactive with 17 years of service credit and an Average Final Compensation of $10,000. This member will have two benefit options at retirement:
>
> - Option 1: 2% x 17 yrs x $10k for a $3400 monthly benefit plus a lump sum of $20,400
> - Option 2: (2% x 15 years + 2.5% x 2years) x $10K for a monthly benefit of $3500 per month

Implementation of a Benefit Improvement using the Benefit Improvement Account

Previous benefit improvements to LEOFF Plan 2 have been paid for through contribution rate increases. The BIA is a new method for funding a benefit improvement and it has never been used. The intent of the BIA was to prefund a benefit improvement so that there would be no impact on contributions. However, the current LEOFF Plan 2 funding policies would result in a contribution rate increase even with enough money in the BIA to fully purchase the benefit improvement.

The Board's strategic plan goals for the funding policy are stable rates and a fully funded plan. To achieve this goal, the Board sets the contribution rate at the greater of the Aggregate Funding Method or the Minimum Rate Funding Policy. Currently, the Minimum Rate Funding Policy is greater than the Aggregate Funding Method. The Minimum Rate Funding Policy is based on the Normal Cost of Entry Age Normal Cost Method (expected long-term cost of the plan excluding the current level of assets). The Minimum Rate Funding Policy contains a rate floor and a rate ceiling based on the funded status of the plan. The floor is set at 100% of the minimum rate if the funded status is equal to or less than 105%. The ceiling is set at 90% of the minimum rate if the funded status exceeds 105%.

Under current funding policies a benefit improvement would result in an increase to liabilities to the plan. There is no current policy for using assets in the BIA to offset that increase in liabilities. Therefore, the Board must determine a policy that allows the assets in the BIA to offset the increase in liabilities caused by a benefit improvement, so there is no increase in required contributions.

Two options for the Board to address this issue are:

1. Fix rates for the remainder of the current biennium and the next biennium according to the Board's current funding policy and develop a policy in consult with OSA that allows the assets in the BIA to offset the increase in liabilities from the benefit improvement so that there is no increase in required contributions; or,
2. Fix rates for the remainder of the current biennium and the next biennium according to the Board's current funding policy and then develop a policy in consult with OSA that would allow the assets in the BIA to offset the increase in liabilities from the benefit improvement such that there is no increase in required contributions.

Option 1 would allow the Board to immediately address the issue. It would also allow OSA to use the new funding policy in its 25-year cost impact for the fiscal note. This would give the legislature the opportunity to see the long-term cost impact of the benefit improvement. However, it does not give much time for the Board to work with OSA to identify and study options.

Option 2 gives the Board time to work with OSA to identify options and then study those options. However, without such a policy in the bill the long-term cost in the fiscal note would reflect current law and as noted above, current law would not reflect the intended rate reductions from the BIA. Therefore, the long-term costs of the bill would not be accurately reflected in the fiscal note for legislation.

POLICY OPTIONS

Lump Sum Benefit:

1. $20,000 lump sum; or,
2. $100 per month of service;
    a. Minimum of $20,000 benefit for catastrophic disability retirees, duty disability retirees, and duty death beneficiaries.

Tiered Multiplier Benefit:

1. Increase multiplier to 2.5% for years of service between 15 and up to 26.

Options for implementation of a benefit:

1. Develop a policy in consult with OSA that allows the assets in the BIA to offset the increase in liabilities from the benefit improvement so that there is no increase in required contributions; or,
2. Fix rates for the remainder of the current biennium and the next biennium according to the Board's current funding policy and then develop a policy in consult with OSA that would allow the assets in the BIA to offset the increase in liabilities from the benefit improvement such that there is no increase in required contributions.

LEOFF

Plan 2 Retirement Board

Tiered Multiplier Benefit Improvement

Comprehensive Report

November 17, 2021

Issue

- A benefit improvement purchased using the Benefit Improvement Account should meet the policy goals of the Law Enforcement Officers' and Fire Fighters' (LEOFF) Plan 2 Board while also adhering to the legislative intent of the Benefit Improvement Account

Background

- In creating the BIA the legislature recognized that:

  > “the current benefit formula and contributions for [LEOFF] 2 are inadequate to modify that formula in recognition of the shorter working careers for firefighters and police officers. […] In recognition of the physical demands of the professions and the inherent risks faced by law enforcement officers and firefighters, eligibility for retirement in [LEOFF] 2 system has been set at age fifty-three. However, the benefit formula is designed for careers of thirty-five to forty years, making retirement at age fifty-three an unrealistic option for many.”

Benefit Formula

- Income replacement standard for retirement is often cited as 60%
- The benefit formula for Washington State administered pension systems, including LEOFF Plan 2, is: 2% x Years of Service x Final Average Salary
- To reach 60% replacement income using this formula a member must have a 30-year career

Average LEOFF 2 Member Benefit

- The average LEOFF Plan 2 retiree replaces approximately 47% of pre-retirement income:
  - Has a Final Average Salary of approximately $10,000 per month
  - Retirees at age 56 with 23.5 years of service
  - Receives a benefit of approximately $4,700 per month

Board's Policy Goals with BIA

- The Board has discussed the following policy goals of purchasing a benefit improvement using the BIA:
  - The benefit should apply as broadly as possible
    - Provide a benefit to as many members as possible while also recognizing the limitations of the cost of the benefit
    - Recognize that retirees helped fund the BIA
    - Prioritize a larger benefit for members who spend a career in LEOFF Plan 2
  - Retention
    - One of the primary goals of any pension plan is to recruit and retain employees
    - Improve retention of LEOFF members

Lump Sum Benefit

1. $20,000 lump sum payment to all retirees
   - Pros - Simple to administer and could be seen as most fair option since everyone gets the same amount
   - Cons - No proportionality to years of service
2. $100 per month of service and a minimum of $20,000 for catastrophic and duty disability retirees, and duty death beneficiaries
   - Pros – Benefit value proportionate to service
   - Cons – More complex to administer

Examples - Option 2

- 5 years of service credit would receive a lump sum payment of $6,000
- 10 years of service credit would receive a lump sum payment of $12,000
- 20 years of service would receive a lump sum payment of $24,000
- 25 years of service would receive a lump sum payment of $30,000

Tiered Multiplier Benefit

- The tiered multiplier benefit would increase the plan benefit multiplier from 2% to 2.5% for the years of service for active members between 15 and up to 26
  - Pros - Improve retirement income so that retirees can be closer to the 60% income replacement goal; incentivizes members to remain in LEOFF Plan 2
  - Cons - Does not provide a benefit to members who work less than 15 years

Who gets which benefit?

Retired as of 2/1/21	
LEOFF 2 Member Group	**Benefit Improvement**
Retired as of 2/1/21	Lump sum
Duty or catastrophic disability retired as of 2/1/21	Lump sum (minimum of $20k)
Beneficiary of line-of-duty death who died prior to 2/1/21	Lump sum (minimum of $20k)
Survivor beneficiary, member deceased as of 2/1/21	Lump sum
Member deceased as of 2/1/21 with no survivor beneficiary	No benefit
Withdrawn	No benefit

LEOFF 2 Member Active as of 2/1/21	
LEOFF 2 Member Group	**Benefit Improvement**
Still active	Choice of lump sum or tiered multiplier
Now retired	Choice of lump sum or tiered multiplier
Duty or catastrophic disability retirement	Choice of lump sum (minimum of $20k) or tiered multiplier
Beneficiary of line-of-duty death who was active as of 2/1/21	Choice of lump sum (minimum of $20k) or tiered multiplier
Survivor beneficiary, member deceased after 2/1/21	Choice between a lump sum or tiered multiplier benefit at retirement
Survivor beneficiary in service death not line-of-duty	Choice of lump sum or tiered multiplier
No survivor beneficiary, member deceased after 2/1/21 before effective date of the bill	Lump sum to beneficiary or estate
No survivor beneficiary in service death not line of duty	Lump sum to beneficiary or estate
Withdrawn	No benefit
Inactive as of 2/1/21 and vested	Choice of lump sum or tiered multiplier
Inactive and not vested	No benefit
Inactive and not vested as of 2/1/21, returns to LEOFF employment after 2/1/21 and becomes vested	Choice of lump sum or tiered multiplier

New Member after 2/1/21	
LEOFF 2 Member Group	**Benefit Improvement**
New members after 2/1/21	Tiered multiplier
Withdrawn	No benefit

Example of Active Member

- Member is currently 45 years old with 20 years of service credit. They work for an additional 10 years and retire at age 55 with an Average Final Compensation of $10,000. This member will have two benefit options at retirement:
- Option 1: 2% x 30 yrs x $10k for a monthly benefit of $6000 plus a lump sum of $36,000
- Option 2: (2% x 20 yrs + 2.5% x 10 yrs) x $10K for a monthly benefit of $6500

Other Decisions

- Date for determining benefits – February 1, 2021
- Option to purchase annuity with lump sum benefit

Implementation

1. Develop a policy in consult with OSA that allows the assets in the BIA to offset the increase in liabilities from the benefit improvement so that there is no increase in required contributions
   - Pros – Allows OSA to use the new policy to identify the long-term costs of the bill
   - Cons – Timeframe is aggressive

2. Fix rates for the remainder of the current biennium and the next biennium according to the Board’s current funding policy and then develop a policy as described in option 1.
   - Pros – Allows time to work with OSA to identify options and for the Board to understand the option
   - Cons – The long-term costs of the bill would not be accurately reflected in the fiscal note

Options

1. Lump Sum Benefit
   a) $20,000 lump sum payment to all retirees with over 5 years of service
   b) $100 per month of service and a minimum of $20,000 for catastrophic and duty disability retirees, and duty death beneficiaries
2. Tiered Multiplier
   a) Increase the plan benefit multiplier from 2% to 2.5% for the years of service between 15 and up to 26
   b) Other
3. Implementation
   a) Develop a policy as part of bill
   b) Fix rates for next three years and then develop a policy

Next Steps

- Final Briefing at December Meeting
  - Staff will draft bill and work with OSA on fiscal analysis
  - Fiscal analysis may not be completed in time for December meeting

Thank You

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Interruptive Military Service Credit

FINAL REPORT

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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.[1] 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[2]; The Persian Gulf War[3]; 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.[4]

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

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[1] 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.

[2] 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.

[3] 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.

[4] 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 SCPP 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[5] 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 SCPP 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

[5] http://leoff.wa.gov/wp-content/uploads/2015/06/121708.6_Interruptive-Military-Service-Credit.pdf

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 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 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.[6]

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 were deployed to the geographic areas where the combat occurred. 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 were not in the geographic area where the actual combat occurred. 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 was 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. [7]

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

[6] 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
[7] 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

Table 1: Categories of CE&S Medals

Title of Decoration[1]	Sub-category of CE&S Medals
Southwest Asia Service Medal[2]	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

Note 1: This list is not all-inclusive. Military Departments also have CE&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.

Note 2: Before DoD established comprehensive CE&S medal policy, the naming conventions for DoD CE&S medals were inconsistent. This resulted in several medals with names that do not match the CE&S medal category to which they are assigned.

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

OSA completed a draft fiscal note (Appendix A) for expanding interruptive military service credit to expeditionary medals across all the state's Plan 2 pension systems and the Washington State Patrol Retirement System (WSPRS). For LEOFF Plan 2, OSA's analysis identified a 2 basis point increase to the member contribution rate, and a one basis point increase to the employer and state contribution rates. OSA also identified 25-year budget impacts across all the retirement plans as $19.6 million.

Impact on Contribution Rates *(Effective 09/01/2022)*				
Fiscal Year 2023 State Budget	**PERS**	**PSERS**	**LEOFF**	**WSPRS**
Employee (Plan 2 or WSPRS)	0.00%	0.00%	0.02%	0.12%
Employer	0.00%	0.00%	0.01%	0.12%
State			0.01%	

Budget Impacts			
(Dollars in Millions)	**2022-2023**	**2023-2025**	**25-Year**
General Fund-State	$0.2	$0.6	$6.1
Local Government	$0.2	$1.0	$9.7
Total Employer	**$0.5**	**$2.0**	**$19.6**

Note: We use long-term assumptions to produce our short-term budget impacts. Therefore, our short-term budget impacts will likely vary from estimates produced from other short-term budget models.

OSA further broke down the budget impacts by retirement plan:

Budget Impacts					
(Dollars in Millions)	**PERS**	**PSERS**	**LEOFF**	**WSPRS**	**Total**
2022-2023					
General Fund	$0.0	$0.0	$0.2	$0.0	$0.2
Non-General Fund	0.0	0.0	0.0	0.1	0.1
Total State	**$0.0**	**$0.0**	**$0.2**	**$0.1**	**$0.3**
Local Government	0.0	0.0	0.2	0.0	0.2
Total Employer	**$0.0**	**$0.0**	**$0.4**	**$0.1**	**$0.5**
Total Employee	**$0.0**	**$0.0**	**$0.4**	**$0.1**	**$0.5**
2023-2025					
General Fund	$0.1	$0.0	$0.4	$0.0	$0.6
Non-General Fund	0.2	0.0	0.0	0.2	0.4
Total State	**$0.3**	**$0.0**	**$0.4**	**$0.3**	**$1.0**
Local Government	0.3	0.0	0.7	0.0	1.0
Total Employer	**$0.7**	**$0.0**	**$1.1**	**$0.3**	**$2.0**
Total Employee	**$0.5**	**$0.0**	**$1.1**	**$0.3**	**$1.9**
2022-2047					
General Fund	$1.1	$0.1	$4.7	$0.2	$6.1
Non-General Fund	1.6	0.0	0.0	2.2	3.9
Total State	**$2.7**	**$0.1**	**$4.7**	**$2.4**	**$9.9**
Local Government	2.7	0.1	6.9	0.0	9.7
Total Employer	**$5.4**	**$0.3**	**$11.6**	**$2.4**	**$19.6**
Total Employee	**$4.1**	**$0.3**	**$11.6**	**$2.4**	**$18.3**

Note: Totals may not agree due to rounding. We use long-term assumptions to produce our short-term budget impacts. Therefore, our short-term budget impacts will likely vary from estimates produced from other short-term budget models.

For LEOFF Plan 2 the general fund impact for 2022-2023 is $0.2 million; for 2023-2025 it is $0.4 million; and the 25 year expect general fund impact is $4.7 million.

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.

POLICY OPTIONS

Option 1: Expand No-Cost Interruptive Military Service Credit

Expand no-cost interruptive military service credit to include service where a member earns an expeditionary medal.

Option 2: No Action

Continue to limit eligibility for no-cost interruptive military service credit to service where a campaign medal was earned and does not include service where an expeditionary medal was earned.

SUPPORTING INFORMATION

Appendix A: OSA Draft Fiscal Note
Appendix B: Bill Draft

Appendix A

SUMMARY OF RESULTS

BRIEF SUMMARY OF PROPOSAL: Expands the definition of veteran to include individuals who received an Expeditionary medal (or badge) during any armed conflict.

COST SUMMARY

Impact on Contribution Rates *(Effective 09/01/2022)*				
Fiscal Year 2023 State Budget	**PERS**	**PSERS**	**LEOFF**	**WSPRS**
Employee (Plan 2 or WSPRS)	0.00%	0.00%	0.02%	0.12%
Employer	0.00%	0.00%	0.01%	0.12%
State			0.01%	

Budget Impacts			
(Dollars in Millions)	**2022-2023**	**2023-2025**	**25-Year**
General Fund-State	$0.2	$0.6	$6.1
Local Government	$0.2	$1.0	$9.7
Total Employer	**$0.5**	**$2.0**	**$19.6**

Note: We use long-term assumptions to produce our short-term budget impacts. Therefore, our short-term budget impacts will likely vary from estimates produced from other short-term budget models.

HIGHLIGHTS OF ACTUARIAL ANALYSIS

- We estimate this proposal will have a cost to the impacted plans because more members are expected to receive fully subsidized IMSC and consequently larger pension benefits.
  - We expect the impacts of this proposal are immaterial to all plans in TRS and SERS, as well as PERS 1 and LEOFF 1.
- To estimate the cost of this proposal, we primarily relied on data from DRS regarding IMSC granted in the past for Campaign medals.
  - Based upon data from the DoD, we assumed IMSC for Expeditionary medals will be granted at a rate approximately 25 percent lower relative to Campaign medals.
- The actual amount of IMSC granted under this proposal is heavily dependent on the levels of troop engagement and medals awarded. This includes both (1) future unknown conflicts, and (2) members who earned an Expeditionary medal in the past but did not purchase partially subsidized IMSC upon return. As a result, the cost of this proposal could be significantly higher (or lower) than assumed.
  - This proposal is not expected to materially increase the affordability and solvency risks of the plans.

The analysis presented in this draft fiscal note does not include the changes to economic assumptions as adopted by the Pension Funding Council during their October meeting. If this proposal is submitted during the 2022 Legislative Session, we expect an increase in costs due to these assumption changes.

See the remainder of this draft fiscal note for additional details on the summary and highlights presented here.

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WHAT IS THE PROPOSED CHANGE?

Summary of Proposal

This proposal impacts the following systems:

- Public Employees' Retirement System (PERS).
- Teachers' Retirement System (TRS).
- School Employees' Retirement System (SERS).
- Public Safety Employees' Retirement System (PSERS).
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF).
- Washington State Patrol Retirement System (WSPRS).

This proposal expands the definition of veteran in subsection (2)(g) of the Revised Code of Washington (RCW) 41.04.005 to include any participant who was awarded the respective Expeditionary medal (or badge). This change expands the eligibility criteria for certain retirement system benefits (e.g., Interruptive Military Service Credit [IMSC]).

Based on their administrative interpretation of the proposal, the Department of Retirement Systems (DRS) has determined this proposal would apply as follows:

- Members who purchased partially subsidized service credit and whose service meets the new eligibility requirements would receive a refund of their member contributions for any prior payment.
- Increase in Pension Benefit Prospectively:
  - Fully subsidized IMSC will be provided to eligible members who were awarded an Expeditionary medal (or badge); however, did not purchase partially subsidized military service upon returning to their DRS-covered position.
  - Fully subsidized IMSC will be provided to eligible members awarded Expeditionary medals (or badges) in the future.

Assumed Effective Date: 90 days after session.

What Is the Current Situation?

The definition of "veteran" in RCW 41.04.005 is used to determine eligibility for pension benefits related to military service credit for all plans. This definition is also used for other purposes, but only the impacts to pension benefits are covered in this draft fiscal note.

To qualify as a veteran under this statute, a member must have either:

- ❖ Served during one of the wars listed (e.g., World War II); or
- ❖ Been awarded the respective Campaign medal (or badge) for any armed conflicts (e.g., the invasions of Grenada or Panama, etc.).

Campaign and Expeditionary medals recognize service members for participation in military campaigns and expeditions, and significant military operations. Eligibility and criteria are based on a service member's degree of personal risk and hardship, participation in designated military operations, and the extent of service during specified time periods.

- ❖ Campaign medals are associated with the highest level of personal risk and hardship. These medals recognize deployed participation in large-scale or long-duration combat operations and are awarded to service members who are deployed to the geographic areas where combat is occurring.
- ❖ Expeditionary medals are associated with high levels of personal risk and hardship. These medals recognize deployed participation in small scale and/or short duration combat operations or military operations where there is an imminent threat of hostilities. These medals are also awarded to members deployed in support of combat operations, but who are not in the geographic area where combat is occurring.

Interruptive Military Service Credit

Members of PERS, TRS, SERS, PSERS, LEOFF, and WSPRS qualify for IMSC when they take a leave of absence from their DRS-covered position to serve in the United States military and return to work within 90 days of honorable discharge.

Members can receive up to ten years of IMSC of which:

- ❖ Up to five years at no cost to the member (i.e., fully subsidized) if the member's service took place during a period of war or an armed conflict during which a Campaign medal (or badge) was earned.
- ❖ Up to five years can be purchased by the member (i.e., partially subsidized) if their military service did not take place during a period of war. In this scenario, the member pays the member contribution cost for those years.

Additionally, in the event a member dies while honorably serving in the national guard or military reserves during a period of war, the member's beneficiary or estate is entitled to the following:

- ❖ For PERS, TRS, SERS, or PSERS: Retirement allowance is not subject to actuarial reduction.

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- For LEOFF or WSPRS: Duty-related death benefits provided in the respective plan.

Non-Interruptive Military Service Credit

PERS 1 and WSPRS 1 also have provisions for non-interruptive military service credit. After completing 25 Years of Service (YOS) credit in these plans, members with service in the armed forces (as defined in RCW 41.04.005) may be credited up to five years of military service whether or not they left the employment of a participating employer to serve.

Who Is Impacted and How?

This proposal could affect all current and future members of the impacted plans through improved benefits by changing the definition of veteran for fully subsidized IMSC. In other words, the definition of veteran is expanded to cover all members who were awarded an Expeditionary medal.

The benefits of eligible members can be improved in two ways:

1. **Increase in Pension Benefit:** This proposal will increase the pension benefits by providing additional service credit to members who were awarded an Expeditionary medal in the past or are awarded this medal in the future.

   For example, a Plan 2 member who retires with an average final salary of $100,000 and 25 YOS under current law will receive an initial annual benefit of $50,000 per year at retirement. If the same member had six months of fully subsidized IMSC, then their annual benefit would be 2.0 percent larger (i.e., $51,000).

   Members who were awarded an Expeditionary medal and purchased IMSC will not see a pension benefit increase; see bullet 2 below for how they'll be impacted.
2. **Return of Contributions:** Impacted members who already purchased IMSC will have their past payment(s) reimbursed by DRS.

This proposal impacts all employers and Plan 2 members through increased contribution rates. With the exception of WSPRS members[1], this proposal will not affect member contribution rates in Plan 1 since they are fixed in statute. Additionally, this proposal will not affect member contribution rates in Plans 3 since they do not contribute to their employer-provided defined benefit.

There could be a limited number of impacted members currently in PERS 1, TRS 1, and LEOFF 1 that may receive increased benefits. Any increase in costs to these plans would be funded according to the plan's funding policy.

[1] *WSPRS 1 members have the same contribution rate as Plan 2 members.*

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WHY THIS PROPOSAL HAS A COST AND WHO PAYS FOR IT

Why This Proposal Has a Cost

This proposal allows members to receive fully subsidized IMSC for military service not covered under current law. As a result, an eligible member who applies for, and receives, IMSC will have a larger benefit upon retirement.

In addition, eligible members who already purchased IMSC will have their past payment(s) reimbursed by DRS. Any reimbursement of past payments would decrease assets of the plan which ultimately results in a cost.

Who Will Pay for These Costs?

PERS, TRS, SERS Plans 2/3 and PSERS Plan 2

Where applicable, the costs that result from this proposal will be divided between members and employers according to standard funding methods that vary by plan:

- Plan 1: 100 percent employer.
- Plan 2: 50 percent member and 50 percent employer.
- Plan 3: 100 percent employer.

LEOFF 2

Any costs that arise from this proposal will be divided according to the standard funding method for LEOFF Plan 2: 50 percent member, 30 percent employer, and 20 percent state.

WSPRS Plans 1/2

This proposal constitutes a benefit improvement. As a result, any unfunded costs that arise from this proposal will be divided according to the standard funding method of 50 percent member and 50 percent employer. The statutory maximum member contribution rate will correspondingly increase as well. The current maximum member rate is 8.61 percent. A supplemental rate, due to this proposal, would increase the maximum by 0.12 percent.

Plan 1 (PERS, TRS, LEOFF)

PERS, SERS, and PSERS employers will realize any impacts on the PERS 1 Unfunded Actuarial Accrued Liability (UAAL) payments, whereas TRS employers will realize any impacts on the TRS 1 UAAL payments. We expect no impact to contribution rates in LEOFF 1 given the small number of active members and the current funded status in LEOFF 1.

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HOW WE VALUED THESE COSTS

Special Data Needed

We relied on data from DRS and the Department of Defense (DoD) to help inform the assumptions we selected. The DRS data was used to identify the number of Washington State retirement system members that are annually awarded fully subsidized IMSC for Campaign medals. While the DoD data was used to compare the number of Expeditionary medals awarded relative to Campaign medals at the national level.

We reviewed this historical data and found it reasonable for the purposes of this proposal, but we did not audit the data. We assumed the data was accurate and complete. Please see **Appendix A** for more details.

Otherwise, we developed these costs using the same assets and data as disclosed in the *June 30, 2019, Actuarial Valuation Report* (AVR).

Assumptions We Made

Separate assumptions were made to value the service credit expected to be earned in the future as well as service credit earned in the past.

These two sets of costs (for future and historical service credit) were combined to form the overall expected cost of this proposal.

Assumptions for Future Service Credit

We set a "load" to value our expectations for IMSC, via Expeditionary medals, to be earned in the future. The load represents a percentage increase that is intended to capture the impact of granting fully subsidized IMSC that is not captured under current law. In order to model the increase in expected costs from this proposal, we applied a load to the active retirement benefits within our valuation software; we think this is appropriate given that approximately 90 percent of our active member plan obligations are attributable to retirement.

To begin setting this load for future service credit, we reviewed the data provided by DRS on historical fully subsidized IMSC granted to eligible members who earned a Campaign medal over a ten-year period (2010-2019). We believe it's reasonable to expect these average levels of IMSC granted in the past to continue in the future. For this reason, we relied on this experience to help develop our load assumption for Expeditionary Medals.

The following bullet points outline the calculation of our method for developing a best estimate load, followed by a table with by-plan data and the results of those calculations.

1. Annual Percent of Population Receiving Fully Subsidized IMSC (a / b).
   a. Average Number of Members who Received IMSC Annually.
   b. Average Number of Active Members in the Plan.

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2. Adjustment for Estimated Average Future Years of Service.
3. Percent of Current Actives Expected to Receive IMSC over the Career (Step 1 x Step 2).
4. Average IMSC Granted Per Eligible Member.
5. Average Expected YOS at Retirement.
6. Preliminary Assumed Load (Step 3 x Step 4 / Step 5).
7. Adjustment for Expected Frequency of Expeditionary vs. Campaign medals.
8. Final Assumed Load (Step 6 x Step 7).

Calculation of Best Estimate Load: Future IMSC *(Expeditionary Medals)*					
Observed DRS Data from 2010-2019	**PERS 2/3**	**PSERS**	**LEOFF 2**	**WSPRS 1**	**WSPRS 2**
1) Annual Percent of Population Impacted (a / b)	**0.0%**	**0.0%**	**0.2%**	**0.9%**	**0.2%**
a. Average Impacted Member Count*	34	2	32	6	1
b. Average Count of Actives	150,743	5,243	17,235	591	453
2) Adjustment for Estimated Future Service *(In Years)***	5	8	8	2	13
3) Percent Expected to Receive IMSC (1 x 2)	**0.1%**	**0.3%**	**1.5%**	**1.9%**	**2.3%**
4) Average IMSC Granted	1.0	0.6	0.8	0.8	0.8
5) Average Expected YOS at Retirement	23	19	28	28	25
6) Preliminary Assumed Load (3 x 4 / 5)	**0.0010%**	**0.0013%**	**0.0053%**	**0.0256%**	**0.0061%**
7) Adjustment for Expected Frequency***	-25%	-25%	-25%	-25%	-25%
8) Final Assumed Load (6 x 7)	**0.0038%**	**0.0077%**	**0.0320%**	**0.0385%**	**0.0594%**

**DRS members given fully subsidized IMSC for Campaign medals.*
***See Adjustment for Estimated Future Service, below, for details.*
****See Adjustment for Expected Frequency, below, for details.*

Two adjustments were made to the load assumption:

1. **Adjustment for Estimated Future Service:** The Annual Percent of Population Impacted only captures the number of members expected to be awarded IMSC, via Campaign medals, in the next year. Given this, an adjustment was made reflecting the average number of years we expect the current active population to continue earning IMSC in the future, but limited to age 50.

    a. For this analysis, we selected age 50 as the cut off because as members approach retirement, we think it's unlikely that they will interrupt their careers to temporarily join the military. Given that the youngest retirement-eligible age is 50 for LEOFF 2, we decided that could be an appropriate upper end for all systems when estimating the average number of future years the current active population would continue to accrue IMSC. This assumption is supported by the following linked study by the PEW Research Center which indicates that only about one-in-ten active military are older than age 40.

2. **Adjustment for Expected Frequency:** We expect Expeditionary medals will be awarded at a pace approximately 25 percent lower than Campaign medals. This downward adjustment was set based on DoD

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data summarized in **Appendix A** which shows an Expeditionary to Campaign medal ratio of 0.75 over approximately the last 20 years.

Assumptions for Historical Service Credit

Members who were awarded an Expeditionary medal in the past are also impacted under this proposal. These members will receive either a return of contributions by virtue of paying for partially subsidized IMSC or an increase in future pension benefits. The assumptions within this section focus on the costs of the population who will have an increase in future pension benefits (since so few partially subsidized members exist within the DRS data). These members were previously eligible to purchase IMSC; however, they may have elected to not do so and consequently we do not have any data on them.

We used the following methods to estimate their cost under this proposal:

- We began by estimating the value of the fully subsidized IMSC for Campaign medals over this period.
  - We calculated a liability per year of service by taking the total active Present Value of Future Benefits (PVFB) for each plan (from the 2019 AVR) and dividing by the expected YOS at retirement for future retirees (i.e., the same as number 5 in the Calculation of Best Estimate Load table above). This amount was then multiplied by the fully subsidized IMSC granted for the observed time period of 2010 through 2019. Our understanding is that Expeditionary medals have primarily been granted since 2001, so we doubled this cost for most systems (except PSERS, given its plan maturity).
- Similar to the Assumptions for Future Service Credit section, we relied on data for Campaign medals but applied a 25 percent downward adjustment to reflect Expeditionary medals being awarded at a slower rate.
- Based on this methodology, we estimate the following fully accrued costs are attributable to historical IMSC for Expeditionary medals.

Cost Attributable to Historical Service				
Dollars in Millions	PERS 2/3	PSERS	LEOFF 2	WSPRS
PVFB	$4.6	$0.1	$8.1	$2.3

While this estimate for historical service costs is being applied based upon the average active member, we recognize that some recipients may already be retired. That said, they won't receive retroactive payments back to the date of their retirement, so we believe this approach is reasonable.

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Other Assumptions

Our analysis does not include any contributions for fully subsidized IMSC that would be made by impacted employers. These payments would reduce the overall cost to the system (at the expense of the contributing employer), so we do not believe it is material to the overall budget impact of this proposal.

We anticipate the impact to duty-related death benefits under this proposal is not material to this pricing exercise, and as a result we have not captured any associated cost in this draft fiscal note. Similarly, we do not expect refund of past payments for eligible members who purchased partially subsidized IMSC will materially impact this draft fiscal note.

We assume the impact to all plans in TRS and SERS, as well as PERS 1 and LEOFF 1, are immaterial under this proposal. Few members of these plans, relative to active membership, have qualified for IMSC in the past, so we assume that will continue under this proposal.

Otherwise, we developed these costs using the same assumptions as disclosed in the AVR, Projection Disclosures, and the *2016 Risk Assessment Assumptions Study* (RAAS) available on our website.

How We Applied These Assumptions

The fiscal impact of this proposal represents the change in projected contributions. To estimate the fiscal impact of this proposal, we compared projected pension contributions under current law to the projected contributions we expect under this proposal. The projected pension contributions reflect contributions from the current members as well as future hires. For more detail, please see **Appendix B**.

Otherwise, we developed these costs using the same methods as disclosed in the AVR.

ACTUARIAL RESULTS

How the Liabilities Changed

This proposal will impact the actuarial funding of the affected plans by increasing the PVFB. The impact of the increasing liabilities payable for current members is shown in the following table.

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Impact on Pension Liability			
(Dollars in Millions)	**Current**	**Increase**	**Total**
Actuarial Present Value of Projected Benefits *(The Value of the Total Commitment to All Current Members)*			
PERS 2/3	$51,593	$5.7	$51,599
PSERS 2	$1,391	$0.2	$1,391
LEOFF 2	$16,096	$11.3	$16,107
WSPRS 1/2	$1,589	$2.6	$1,592
Unfunded Entry Age Accrued Liability *(The Value of the Total Commitment to All Current Members Attributable to Past Service that is Not Covered by Current Assets)*			
PERS 2/3	$1,833	$5.4	$1,839
PSERS 2	($6)	$0.1	($5)
LEOFF 2	($1,302)	$10.2	($1,292)
WSPRS 1/2	$70	$2.5	$72

Note: Totals may not agree due to rounding.

How the Assets Changed

This proposal would result in a change in assets, but the impact was not captured in this analysis. Assets will decrease as a result of any refunds of past payments for partially subsidized IMSC; at the same time, the assets will increase due to employer payments for future fully subsidized IMSC. Please see the Other Assumptions section above for details.

How the Present Value of Future Salaries (PVFS) Changed

This proposal does not change the PVFS, so there is no impact on the actuarial funding of the affected plans due to PVFS changes.

How Contribution Rates Changed

During Fiscal Year 2023, a supplemental contribution rate is collected for LEOFF 2 and WSPRS 1/2 to fund the cost of this proposal; that cost is shared equally between members and employers. Further, this proposal is a benefit improvement so an increase in WSPRS member maximum contribution rate would also occur.

The increase in the required actuarial contribution rate does not round up to the minimum supplemental contribution rate of 0.01 percent for PERS 2/3 and PSERS 2. Therefore, this proposal will not affect contribution rates in the current biennium for these plans.

We will use the unrounded rate increase shown in the following table to measure the budget changes in future biennia for all impacted plans.

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Impact on Contribution Rates				
System/Plan	**PERS**	**PSERS**	**LEOFF**	**WSPRS**
Current Members				
Employee (Plan 2 or WSPRS)	0.0033%	0.0016%	0.0235%	0.1202%
Employer	0.0033%	0.0016%	0.0141%	0.1202%
State			0.0094%	
New Entrants*				
Employee (Plan 2 or WSPRS)	0.0002%	0.0004%	0.0023%	0.0054%
Employer	0.0002%	0.0004%	0.0014%	0.0054%
State			0.0009%	

*Rate change applied to future new entrant payroll and used to determine budget impacts only. Current members and new entrants pay the same contribution rate.

How This Impacts Budgets and Employees

Budget Impacts					
(Dollars in Millions)	**PERS**	**PSERS**	**LEOFF**	**WSPRS**	**Total**
2022-2023					
General Fund	$0.0	$0.0	$0.2	$0.0	$0.2
Non-General Fund	0.0	0.0	0.0	0.1	0.1
Total State	**$0.0**	**$0.0**	**$0.2**	**$0.1**	**$0.3**
Local Government	0.0	0.0	0.2	0.0	0.2
Total Employer	**$0.0**	**$0.0**	**$0.4**	**$0.1**	**$0.5**
Total Employee	**$0.0**	**$0.0**	**$0.4**	**$0.1**	**$0.5**
2023-2025					
General Fund	$0.1	$0.0	$0.4	$0.0	$0.6
Non-General Fund	0.2	0.0	0.0	0.2	0.4
Total State	**$0.3**	**$0.0**	**$0.4**	**$0.3**	**$1.0**
Local Government	0.3	0.0	0.7	0.0	1.0
Total Employer	**$0.7**	**$0.0**	**$1.1**	**$0.3**	**$2.0**
Total Employee	**$0.5**	**$0.0**	**$1.1**	**$0.3**	**$1.9**
2022-2047					
General Fund	$1.1	$0.1	$4.7	$0.2	$6.1
Non-General Fund	1.6	0.0	0.0	2.2	3.9
Total State	**$2.7**	**$0.1**	**$4.7**	**$2.4**	**$9.9**
Local Government	2.7	0.1	6.9	0.0	9.7
Total Employer	**$5.4**	**$0.3**	**$11.6**	**$2.4**	**$19.6**
Total Employee	**$4.1**	**$0.3**	**$11.6**	**$2.4**	**$18.3**

Note: Totals may not agree due to rounding. We use long-term assumptions to produce our short-term budget impacts. Therefore, our short-term budget impacts will likely vary from estimates produced from other short-term budget models.

The analysis of this proposal does not consider any other proposed changes to the systems. The combined effect of several changes to the systems could exceed the sum of each proposed change considered individually.

Comments on Risk

Our office performs annual risk assessments to help us demonstrate and assess the effect of unexpected experience on pension plans. The risk assessment allows us to measure how affordability and funded status can change if investment experience, expected state revenue growth, and inflation do not match our long-term assumptions. Our annual risk assessment also considers past practices, for funding and benefit enhancements, and their impact on pension plan risk if those practices continue. For more information, please see our Risk Assessment and Commentary on Risk webpages. Additional information on the assumptions used to produce the risk measures can be found in the RAAS.

We would not expect a significant increase to current total plan membership service and consequently the overall risk measures as a result of this proposal. However, an unexpected and significant number of members could earn fully subsidized IMSC if (1) a large-scale and lengthy future conflict were to occur, or (2) if more members earned Expeditionary medals in the past than anticipated.

HOW THE RESULTS CHANGE WHEN THE ASSUMPTIONS CHANGE

The best estimate results can vary under a different set of assumptions. The actual amount of fully subsidized IMSC added as a result of this proposal could be higher (or lower) than we assume. In this section, we summarize some of the reasons why the costs could be more (or less) than what is presented in this draft fiscal note.

- **Future Service:** The actual amount of fully subsidized IMSC granted in the future is heavily dependent on the levels of troop engagement in, and medals awarded for, unknown conflicts down the road. In general, we assumed future annual IMSC will be granted at a frequency similar to what was observed in the DRS data between 2010 and 2019. Actual levels of service granted for future IMSC through Expeditionary medals may be higher (or lower) than our best estimate assumptions and will increase (or decrease) the cost of this proposal.

  For context, we estimate future service is approximately one-third of the cost of this proposal.

- **Historical Service:** We did not have data on members who earned an Expeditionary medal but elected to not purchase partially subsidized IMSC between 2001 and 2019. For this reason, we relied on experience for Campaign medals to help inform our assumptions. Actual levels of service granted for past IMSC through Expeditionary medals may be higher (or lower) than our best estimate assumptions and will increase (or decrease) the cost of this proposal.

  For context, we estimate historical service is approximately two-thirds of the cost of this proposal.

- **Ratio of Expeditionary to Campaign Medals:** We relied on Campaign medal data to help set our assumptions since we expect Expeditionary medals will occur at similar, but 25 percent lower, frequency. This

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expectation is based on total DoD data over the period from 2001 through 2019. We feel this approach is reasonable but will note that this relationship displayed some volatility over the observed time period. For example, 2006-2014 data displayed four Expeditionary medals for every ten Campaign medals; however, 2015-2019 data displayed fourteen Expeditionary medals for every ten Campaign medals. More (or less) Expeditionary medals relative to Campaign medals would increase (or decrease) the cost of this proposal.

WHAT THE READER SHOULD KNOW

The Office of the State Actuary ("we") prepared this draft fiscal note based on our understanding of the proposal as of the date shown in the footer. We intend this draft fiscal note to be used by the LEOFF 2 Board and SCPP during the 2021 Interim for purposes of making recommendations to the 2022 Legislature on this proposal.

We performed this analysis using ProVal® software developed by Winklevoss Technologies. We believe the use of this software is appropriate for purposes of this pricing. Please see page 22 of our [2020 AVR](2020 AVR) for details.

We advise readers of this draft fiscal note to seek professional guidance as to its content and interpretation, and not to rely upon this communication without such guidance. Please read the analysis shown in this draft fiscal note as a whole. Distribution of, or reliance on, only parts of this draft fiscal note could result in its misuse and may mislead others.

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ACTUARY'S CERTIFICATION

The undersigned hereby certifies that:

1. The actuarial cost methods are appropriate for the purposes of this pricing exercise.
2. The actuarial assumptions used are appropriate for the purposes of this pricing exercise.
3. The data on which this draft fiscal note is based are sufficient and reliable for the purposes of this pricing exercise.
4. Use of another set of methods, assumptions, and data may also be reasonable, and might produce different results.
5. The risk analysis summarized in this draft fiscal note involves the interpretation of many factors and the application of professional judgment.
6. We prepared this draft fiscal note for the LEOFF 2 Board and SCPP during the 2021 Interim.
7. We prepared this draft fiscal note and provided opinions in accordance with Washington State law and accepted actuarial standards of practice as of the date shown in the footer of this draft fiscal note.

The undersigned, with actuarial credentials, meets the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

While this draft fiscal note is meant to be complete, the undersigned is available to provide extra advice and explanations as needed.

Michael Harbour

Michael T. Harbour, ASA, MAAA
Actuary

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APPENDIX A – SPECIAL DATA NEEDED

Data from DRS and DoD was used to help inform the assumptions we selected for this pricing exercise. We summarized the information we relied on within this section.

Data from DRS

We reviewed recent historical data from DRS on fully subsidized IMSC granted for Campaign medals. The following table provides an annual summary of the data provided by DRS, as well as the average over the 2010-2019 time period.

IMSC Granted for Campaign Medals

PERS 2/3	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Avg
Count	37	37	23	74	49	46	20	25	19	14	**34**
Avg Service	1.0	1.0	1.2	1.0	1.1	0.7	0.9	0.9	1.2	0.9	**1.0**
PSERS	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**Avg**
Count	1	2	1	8	0	0	4	2	0	3	**2**
Avg Service	0.8	0.6	1.5	0.5	N/A	N/A	0.3	0.9	N/A	0.9	**0.6**
LEOFF 2	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**Avg**
Count	51	54	22	36	42	47	28	19	7	14	**32**
Avg Service	0.9	0.7	1.0	0.8	0.8	0.8	0.7	0.8	0.9	0.8	**0.8**
WSPRS 1	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**Avg**
Count	5	4	4	10	9	4	4	3	4	9	**6**
Avg Service	0.7	0.7	0.8	1.0	0.7	0.5	1.1	1.0	0.5	0.6	**0.8**
WSPRS 2	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**Avg**
Count	1	3	0	0	2	0	1	0	0	1	**1**
Avg Service	0.1	0.4	N/A	N/A	1.1	N/A	1.0	N/A	N/A	1.7	**0.8**

We reviewed the data for TRS and SERS Plans 2/3 but did not include it in the above table. On average, three members (or less) received IMSC annually, which is less than 0.005 percent of their respective active populations.

Data for PERS 1, TRS 1, and LEOFF 1 was also excluded from the above table. These plans closed to new hires in 1977, so the remaining active members would have a least 24 YOS by 2001. Given the accrued service of these plan members, we do not expect a significant number of members would temporarily leave their careers and earn IMSC since they are at, or near, eligibility for retirement.

This data was received from DRS on July 14, 2020, and was initially used for the 2020 Interim *IMSC Study* that was submitted to the Select Committee on Pension Policy as part of SHB 2544. We believe this data remains reasonable for purposes of pricing this proposal. If this proposal becomes a law, then we may request new data to set assumptions for our actuarial valuation.

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Data from DoD

The DoD data in the following table was used to compare the number of Expeditionary medals awarded relative to Campaign medals at the national level. This information was received late 2020 and compiled as part of the *IMSC Study*.

Department of Defense			
	Expeditionary Medals	Campaign Medals	Ratio
2001	4,275	1,276	3.35
2002	3,386	1,306	2.59
2003	7,187	4,463	1.61
2004	19,683	7,001	2.81
2005	31,256	15,652	2.00
2006	9,328	17,255	0.54
2007	7,285	17,002	0.43
2008	8,145	42,847	0.19
2009	9,390	36,791	0.26
2010	10,580	46,362	0.23
2011	16,091	46,305	0.35
2012	16,746	43,674	0.38
2013	19,635	40,020	0.49
2014	21,745	31,825	0.68
2015	36,737	24,108	1.52
2016	27,801	24,704	1.13
2017	48,596	22,478	2.16
2018	31,886	27,797	1.15
2019	23,899	18,793	1.27
Total	**353,651**	**469,659**	**0.75**

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APPENDIX B – HOW WE APPLIED THESE ASSUMPTIONS

We estimated the fiscal impact of this proposal by comparing projected pension contributions under this proposal to contributions under current law. The projected pension contributions reflect contributions from the current members as well as future hires.

To determine the projected contributions under current law, or the “base”, we relied on the AVR. For current members, contribution rates from the AVR are multiplied by future payroll. For future hires, contribution rates under the Entry Age Normal Cost method are multiplied by future new entrant payroll.

To determine the projected costs under this proposal, we modified the base as described above to reflect the provisions of the proposal, the assumptions, and data noted in the body of this draft fiscal note. We then multiplied the respective new contribution rates reflecting these changes by future payroll.

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GLOSSARY OF ACTUARIAL TERMS

Actuarial Accrued Liability: Computed differently under different funding methods, the actuarial accrued liability generally represents the portion of the present value of fully projected benefits attributable to service credit that has been earned (or accrued) as of the valuation date.

Actuarial Present Value: The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of actuarial assumptions (i.e., interest rate, rate of salary increases, mortality, etc.).

Aggregate Funding Method: The Aggregate Funding Method is a standard actuarial funding method. The annual cost of benefits under the Aggregate Method is equal to the normal cost. Under this method, all plan costs (for past and future service credit) are included under the normal cost. Therefore, the method does not produce an unfunded actuarial accrued liability outside the normal cost. It's most common for the normal cost to be determined for the entire group rather than on an individual basis for this method.

Entry Age Normal Cost Method (EANC): The EANC method is a standard actuarial funding method. The annual cost of benefits under EANC is comprised of two components:

- Normal cost.
- Amortization of the unfunded actuarial accrued liability.

The normal cost is most commonly determined on an individual basis, from a member's age at plan entry, and is designed to be a level percentage of pay throughout a member's career.

Normal Cost: Computed differently under different funding methods, the normal cost generally represents the portion of the cost of projected benefits allocated to the current plan year.

Projected Benefits: Pension benefit amounts that are expected to be paid in the future taking into account such items as the effect of advancement in age as well as past and anticipated future compensation and service credits.

Unfunded Actuarial Accrued Liability (UAAL): The excess, if any, of the actuarial accrued liability over the actuarial value of assets. In other words, the present value of benefits earned to date that are not covered by plan assets.

Unfunded EAN Liability: The excess, if any, of the present value of benefits calculated under the EAN cost method over the valuation assets. This is the portion of all benefits earned to date that are not covered by plan assets.

Appendix B

BILL REQUEST - CODE REVISER'S OFFICE

BILL REQ. #:	Z-0372.1/22
ATTY/TYPIST:	KS:eab
BRIEF DESCRIPTION:	Concerning interruptive military service credit for members of the state retirement systems.

AN ACT Relating to interruptive military service credit for members of the state retirement systems; and amending RCW 41.04.005.

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

Sec. 1. RCW 41.04.005 and 2020 c 178 s 1 are each amended to read as follows:

(1) As used in this section and RCW 41.16.220, 41.20.050, and 41.40.170 "veteran" includes every person, who at the time he or she seeks the benefits of this section and RCW 41.16.220, 41.20.050, or 41.40.170 has received an honorable discharge, is actively serving honorably, or received a discharge for physical reasons with an honorable record and who meets at least one of the following criteria:

(a) The person has served between World War I and World War II or during any period of war, as defined in subsection (2) of this section, as either:

(i) A member in any branch of the armed forces of the United States;

(ii) A member of the women's air forces service pilots;

(iii) A U.S. documented merchant mariner with service aboard an oceangoing vessel operated by the war shipping administration, the office of defense transportation, or their agents, from December 7, 1941, through December 31, 1946; or

(iv) A civil service crewmember with service aboard a U.S. army transport service or U.S. naval transportation service vessel in oceangoing service from December 7, 1941, through December 31, 1946; or

(b) The person has received the armed forces expeditionary medal, or marine corps and navy expeditionary medal, for opposed action on foreign soil, for service:

(i) In any branch of the armed forces of the United States; or

(ii) As a member of the women's air forces service pilots.

(2) A "period of war" includes:

(a) World War I;

(b) World War II;

(c) The Korean conflict;

(d) The Vietnam era, which means:

(i) 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;

(ii) The period beginning August 5, 1964, and ending on May 7, 1975;

(e) The Persian Gulf War, 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;

(f) 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

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

--- END ---

LEOFF
Plan 2 Retirement Board

Interruptive Military Service Credit

Final Report
November 17, 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

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

Example 1 – Active members

- An active LEOFF 2 member takes leave from their LEOFF position for military service, earns an expeditionary medal for their military service, and returns to their LEOFF position
- Under this proposal this member would earn no-cost interruptive military service credit, up to 5 years, for their military service
- Active members who have already purchased subsidized interruptive military service credit for service where they earned an expeditionary medal would receive a refund

Example 2 – 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 3 – 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

2021 Actuarial Fiscal Note

Impact on Contribution Rates *(Effective 09/01/2022)*				
Fiscal Year 2023 State Budget	**PERS**	**PSERS**	**LEOFF**	**WSPRS**
Employee (Plan 2 or WSPRS)	0.00%	0.00%	0.02%	0.12%
Employer	0.00%	0.00%	0.01%	0.12%
State			0.01%	

Budget Impacts			
(Dollars in Millions)	**2022-2023**	**2023-2025**	**25-Year**
General Fund-State	$0.2	$0.6	$6.1
Local Government	$0.2	$1.0	$9.7
Total Employer	**$0.5**	**$2.0**	**$19.6**

Note: We use long-term assumptions to produce our short-term budget impacts. Therefore, our short-term budget impacts will likely vary from estimates produced from other short-term budget models.

SCPP Update

- SCPP received an initial briefing in October
- SCPP is scheduled to receive another briefing in November, and possibly December

Policy Options

- **Option 1: Expand No-Cost Interruptive Military Service Credit**
  - Expand no-cost interruptive military service credit to include service where a member earns an expeditionary medal

- **Option 2: No Action**
  - Continue to limit eligibility for no-cost interruptive military service credit to service where a campaign medal was earned and does not include service where an expeditionary medal was earned

Thank You

Jacob White

Senior Research & Policy Manager

(360) 586-2327

jacob.white@leoff.wa.gov

2020 LEOFF 2 Actuarial Valuation Results

Presentation to:

LEOFF Plan 2 Retirement Board

Mitch DeCamp, Senior Actuarial Analyst

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

November 17, 2021

Today's Presentation

- Background on new off-cycle valuation methods
- Key 2020 Actuarial Valuation Report results
- Informational – No Board action needed today

Office of the State Actuary

I. SUMMARY OF KEY RESULTS

IV. ACTUARIAL ASSUMPTIONS AND METHODS


Office of the State Actuary
"Supporting financial security for generations."
2020

2020 Off-Cycle Valuation

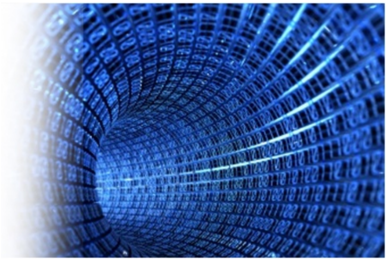
- Under the current contribution rate-setting cycle, even-numbered valuation years (e.g., 2020) are “off-cycle”, or non-rate setting
- “Off-cycle” valuations provide an informational-only update on funding progress and plan developments

New Off-Cycle Valuation Methods

- OSA developed a simplified methods for off-cycle valuations based on the purpose of the report
- How does this impact the 2020 valuation report?
  - Still providing updates on key valuation measures
    - Funded status, liability changes, plan assets
  - Report does not include contribution rates
  - Certain data details are not available

Overview of Methods

- Estimated 2020 data and assets by projecting 2019 data file forward one year
  - Relied on assumptions for changes in the data
  - Adjusted assumptions for actual 2020 salary/membership growth and investment return in projection
  - Compared projection data with actual data to ensure reasonable results
- Testing on prior valuation results using this methodology provided materially identical results



A Couple Important Notes on the 2020 Valuation Results

- The 2020 valuation measures the system at June 30, 2020
- The results from the valuation do not include
  - 2021 Investment Return
  - Economic Assumptions Recommendation

Changes in Market Value of Assets

LEOFF 2		
(Dollars in Millions)	**2019**	**2020***
Beginning Market Value	**$12,985**	**$13,916**
Contributions	393	385
Disbursements	(316)	(363)
Investments	1,154, 8.89%	634, 4.55%
OSA Adjustments**	(300)	0
Ending Market Value	**$13,916**	**$14,573**

Totals may not agree due to rounding.

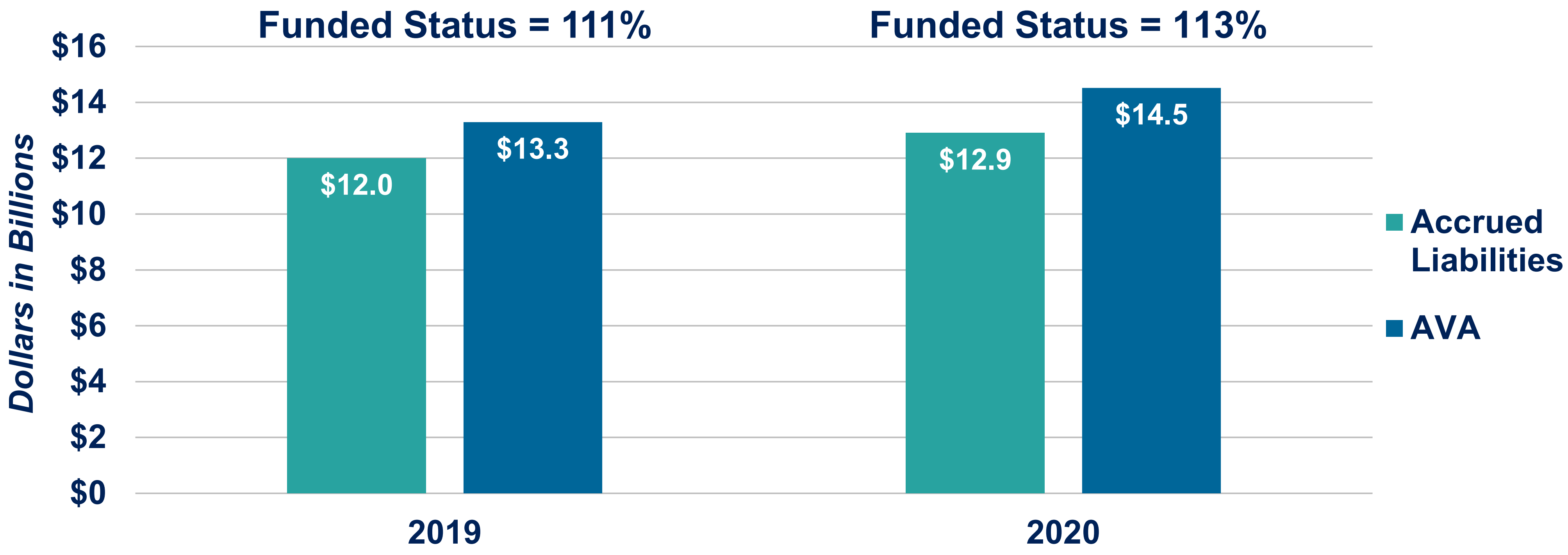
**Estimated figures based on 2020 Actuarial Valuation Report methods.*

***OSA adjusted the market value of assets to reflect transfer of $300 million on July 1, 2019, to the Benefit Improvement Account (BIA).*

Calculating 2020 AVA

Calculation of Actuarial Value of Assets	
(Dollars in Millions)	
Estimated 2020 Market Value (A)	**$14,573**
Deferred Investment Gain/(Loss)	
Plan Year Ending 6/30/2020	($265)
Plan Year Ending 6/30/2019	$0
Plan Year Ending 6/30/2018	$0
Plan Year Ending 6/30/2017	$291
Plan Year Ending 6/30/2016	($83)
Plan Year Ending 6/30/2015	$0
Plan Year Ending 6/30/2014	$110
Total Deferred Investment Gain/(Loss) (B)	**$53**
Estimated 2020 Actuarial Value (A) - (B)	**$14,520**

Funded Status Change from Last Valuation



- Funded Status = $\frac{\text{\$ Actuarial Value of Assets}}{\text{\$ Accrued Liabilities}}$
- If the funded status exceeds 100%, the plan has more than $1 of assets for every $1 of accrued benefits

Office of the State Actuary

Summary of 2020 Actuarial Valuation

- The plan is considered healthy
  - Prior deferred assets offset lower than expected return
  - Funded status exceeds 100%
- 2021 on-cycle valuation will include strong 2021 asset returns and any changes to economic assumptions
  - OSA will present contribution rates June 2022

Questions? Please Contact: The Office of the State Actuary

leg.wa.gov/OSA; state.actuary@leg.wa.gov

360-786-6140, PO Box 40914, Olympia, WA 98504

Mitch DeCamp

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Disclosure

- This presentation is based on the *2020 LEOFF 2 Actuarial Valuation Report*. Please see the report for a full disclosure of assumptions, methods, and data used to produce the results contained in this presentation.

November 17, 2021

Roth 457 / Deferred Compensation Plan Option

COMPREHENSIVE REPORT

By Jacob White
Senior Research & Policy Manager
360-586-2327
jacob.white@leoff.wa.gov

ISSUE STATEMENT

LEOFF Plan 2 members requested a Roth 457 Plan option in the State's Deferred Compensation Plan.

OVERVIEW

The State's Deferred Compensation Plan (DCP) is a tax qualified 457 plan and allows members to make pre-tax deferrals. Some 457 plans allow members to make deferrals after taxes have been paid. These after-tax contributions are call "Roth" contributions. Roth contributions to a 457 plan, along with investment returns on those contributions, are not taxed when a member withdraws them from the plan, so long as the withdrawal is a qualified distribution. The Department of Retirement Systems (DRS) does not include a Roth option in its DCP plans.

BACKGROUND AND POLICY ISSUES

Roth contributions to a 457 plan are made on an after-tax basis and will not reduce a member's income taxes for the year. However, Roth contributions and their associated earnings can be withdrawn tax-free if the requirements for a qualified distribution are met. The earnings from Roth contributions not being taxed is a particularly significant benefit to younger members enrolled in DCP, whose contributions accumulate earnings tax free for a much longer time.

DRS is the Plan Administrator for DCP

DRS is the plan administrator for DCP.[1] As the plan administrator DRS has the authority to implement a Roth option for DCP without legislation. In 2014 the LEOFF Plan 2 Board sent a letter (see Appendix A) to DRS requesting they implement a Roth option within its DCP.

In 2015, DRS presented to the LEOFF Plan 2 Board their intent to implement a Roth option for DCP as part of DRS's strategic planning goals.[2] Initially, DRS cited the implementation of a new DCP Record Keeper as the reason for the delay in providing a Roth option. Since that initial delay, DRS changed DCP Record Keepers a second time. Prior to the LEOFF Plan 2 Board's June 2021 meeting, DRS told the Board they were not going to spend the resources to implement a Roth 457 option at this time.

In July, the Select Committee on Pension Policy (SCPP) received a "Deferred Compensation Overview" briefing from DRS, which included information about why DRS was not offering a Roth option. DRS cited the costs associated with implementation, approximately $640,000, as the main driver for not offering a Roth option (see appendix B). Without legislative funding the costs would be paid by all DCP participants through increased administrative fees, not just those utilizing the Roth option.

Based on the feedback from the LEOFF Plan 2 Board, SCPP, and DRS members, DRS submitted a budget request package to the Governor's Office on September 13, 2021 (see Appendix C). The budget request package identified total implementation costs as $988,430 total over the next two biennia ($609,350 in 2021-23 and $379,080 in 2023-2025). DRS will find out if their budget request was approved when the Governor's Budget is released on December 21, 2021.

Differences between a Roth IRA and a Roth 457

There is often confusion between a Roth Individual Retirement Account (Roth IRA), and a Roth 457 Plan. Both a Roth IRA and a Roth 457 Plan allow for deferrals after taxes have been paid. However, a Roth 457 Plan can only be offered by states, local governments, and certain non-profit organizations to their employees. Any worker can contribute to a Roth IRA if their compensation and modified adjusted gross income fall below certain limits.[3] A Roth IRA cannot be offered through a public employer, instead an employee can set up a Roth IRA through a private investment company or bank.

[1] RCW 41.50.770, https://app.leg.wa.gov/RCW/default.aspx?cite=41.50.770
[2] https://leoff.wa.gov/sites/default/files/2020-02/111815.4_DRS.Update.pdf
[3] Publication 590-A (2020), Contributions to Individual Retirement Arrangements (IRAs) | Internal Revenue Service (irs.gov), https://www.irs.gov/publications/p590a#idm140656789740128

An employee eligible for a Roth 457 Plan may also make deferrals into a Roth IRA. Additionally, Roth 457 plans have higher contribution limits than a Roth IRA. Therefore, while LEOFF Plan 2 members may be able to realize post-tax savings in a private Roth IRA, they cannot save additional post-tax funds in a Roth account without their employer offering a Roth 457 plan.

Pre-Tax and Roth Contributions are not "stackable"

457 plan contribution limits apply to the combination of pre-tax and Roth contributions. For 2020 and 2021, a member under age 50 can contribute up to $19,500 to their 457 plans. A member over age 50 can make an additional $6,500 in catch-up contributions. Roth 457 contributions are not separate from pre-tax 457 contributions for purposes of determining the maximum annual contributions a member can make. Therefore, a member could decide what portion of their maximum 457 contribution amount ($19,500 and $6,500 in catch-up contributions) is pre-tax, post-tax, or a combination of both.

In contrast, Roth IRA contribution limits are separate from 457 plan contribution limits. A 457 plan member could make their maximum 457 contributions ($19,500 and $6,500 in catch-up contributions) and make additional contributions to a Roth IRA ($6,000 regular and $1,000 catch-up contributions).

LEOFF Plan 2 Participation in DCP

Local employers must opt into DCP for their LEOFF Plan 2 members to have the option of participating in DCP. Many LEOFF Plan 2 employers have not opted into DCP. Legislation requiring all public employers to offer DCP to their employees has been unsuccessful in prior sessions, however, the LEOFF Plan 2 Board has not sponsored these bills.

Currently, 18.90% (3,521) of LEOFF Plan 2 members are enrolled in DCP and 67% (354) of LEOFF Plan 2 employers are enrolled into DCP. Of those 354 employers, 40% of their LEOFF Plan 2 members are enrolled in DCP. Based on data from other state plans offering a Roth 457 option, DRS expects approximately 12% of DCP participants, or 423 LEOFF Plan 2 members, to utilize a Roth option.

POLICY OPTIONS

Option 1: No action at this time

The Board may choose to not pursue legislation this session since DRS has submitted a Budget Request with the Governor's Office. The Board will not know whether the Budget Request was included in the Governor's Budget until after the final interim meeting in December.

Option 2: Endorse legislation

The Board may sponsor legislation this session in case DRS's Budget Request is not included in the Governor's Budget or is cut from the final budget passed by the legislature.

SUPPORTING INFORMATION

Appendix A: LEOFF Plan 2 Board Letter to DRS, January 8, 2014.

Appendix B: DRS Presentation to SCPP, July 2021.

Appendix C: DRS Budget Request Decision Package, September 13, 2021.

Appendix A

STATE OF WASHINGTON

LAW ENFORCEMENT OFFICERS' AND FIRE FIGHTERS'
PLAN 2 RETIREMENT BOARD

P.O. Box 40918 - Olympia, Washington 98504-0918 - (360) 586-2320 - FAX (360) 586-2329

January 8, 2014

Marcie Frost, Director
Department of Retirement Systems (DRS)
PO Box 48380
Olympia, WA 98504-8380

Dear Ms. Frost:

We share an interest in helping employees utilize retirement savings options available under federal tax law. I am writing on behalf of the Board to ask DRS to take advantage of recent changes in the Small Business Protection act of 2010 expanding those options.

The LEOFF Plan 2 Board recently reviewed information on recent changes allowing DRS's governmental 457 plans to authorize:

- Roth or after-tax contributions; and
- Conversion of current pre-tax account balances to a Roth account taxable in year of conversion.

Based on the understanding that no enabling legislation is required, the Board voted at its December 18, 2013 meeting to ask DRS to implement these Roth options.

At the request of the Board, please consider developing an implementation plan for offering this option. Thank you for your attention to this issue.

Sincerely,

Kelly L Fox

Kelly Fox, Chair
LEOFF Plan 2 Retirement System Board

Cc: Steve Nelsen, LEOFF Plan 2 Retirement Board
Jane Sakson, Office of Financial Management
Dave Nelsen, Department of Retirement Systems

DEFERRED COMPENSATION PROGRAM OVERVIEW

Seth Miller
Retirement Readiness Director

Select Committee on Pension Policy
July 20, 2021

1

Outline

- DCP overview
- Auto enrollment overview
- Roth 457 considerations

2

DCP overview

- DCP is an optional, additional retirement savings vehicle
- It is an IRC section 457 plan
- All state agencies participate
- Local government employers can also participate or offer their own plan

3

DCP investments

- Investments are selected by the WSIB
- 13 Retirement Strategy Target Date Funds
- 7 Individual "mutual fund" type investments

4

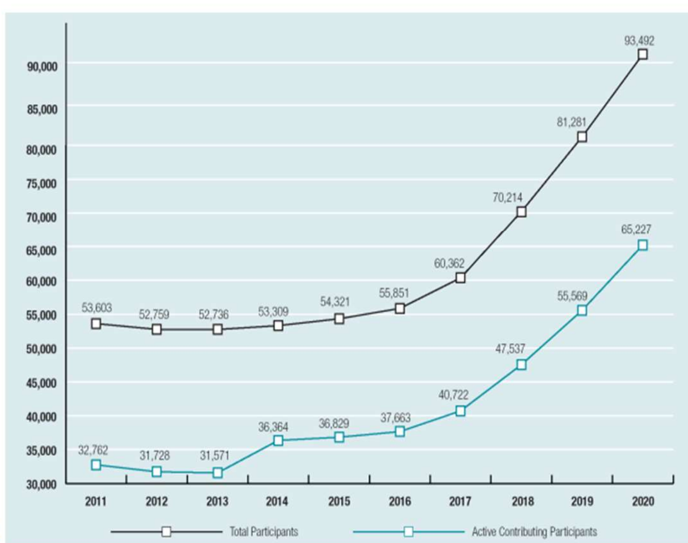
Administration of DCP

- Administrative options are determined by DRS
- Include options such as
  - Choice of Record Keeper
  - Fee structure
  - Loans
  - SECURE Act provisions
  - After-tax contributions (Roth)

WASHINGTON STATE
Department of Retirement Systems

5

Growth in DCP participation

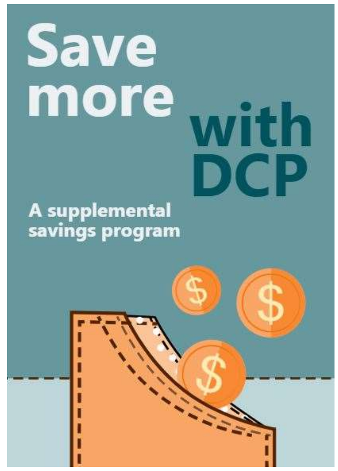


WASHINGTON STATE
Department of Retirement Systems

6

DCP automatic enrollment

- Since January 1, 2017, all newly hired state and higher education employees are automatically enrolled in the state's Deferred Compensation Program



Washington State Department of Retirement Systems

7

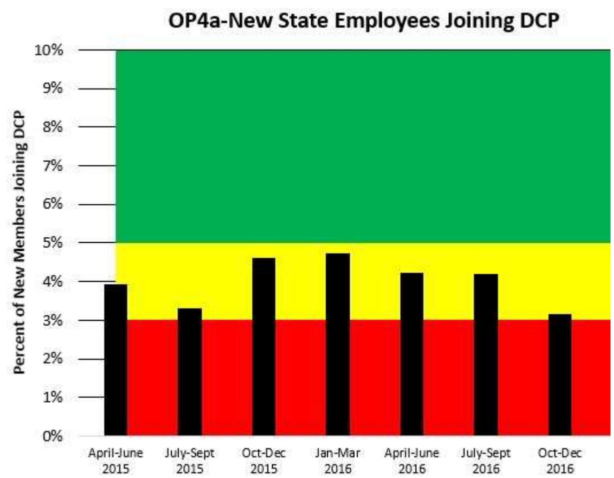
DCP and automatic enrollment basics

- Default contribution rate of 3%
- Default age appropriate Target Date Fund
- Contributions are refunded if member opts out within 90 days

Washington State Department of Retirement Systems

8

DCP – pre-2017 auto enrollment



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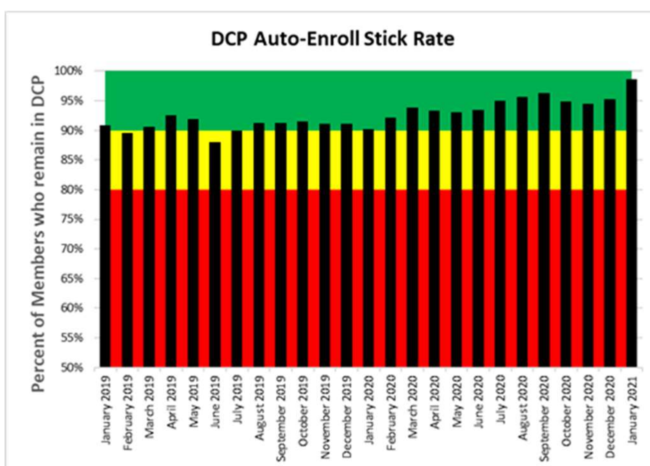
DCP automatic enrollment



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DCP automatic enrollment

- "Stick rate" is 87– 90%
- Average age of DCP participants has dropped from 47 to 42 since auto enrollment

11

Automatic enrollment myths

Lower income workers will be less likely to participate.

- "…stats get even more impressive when looking at participation rates among minorities and lower income workers. "
- DRS has seen similar results in our own data.

Reference: https://www.pai.com/blog/benefits-of-automatic-enrollment-in-a-retirement-plan

12

Roth 457

- Since 2011 457 plans have been able to offer a "Roth" option
- Contributions are made after-tax
- Contributions and investment returns are not taxed at time of withdrawal

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Roth IRA vs Roth 457

- Roth IRA
  - A private option - doesn't matter who your employer is
  - Workers who earn under a certain amount can contribute
  - $6000 yearly limit if under age 50
- Roth 457 Plan
  - Can only be offered by states, local governments, and certain not profit organizations to their employees
  - No income limit to make contributions
  - $19,500 contribution limit for those under age 50

14

Why DRS currently does not offer a Roth 457 option

- Previous related implementations of higher priority
  - Auto enrollment
  - New Employer Reporting Application
  - Record Keeper transitions
- Generally low take up rates for Roth options
  - 12% of employees in 401(k) plans
  - Limited but vocal interest from participants
- Added complexity for both employers and customers

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Other considerations

- Cost/Effort of implementation
  - Internally developed DRS fiscal note estimates an implementation cost of approximately $640,000
  - Without legislative funding, cost would be paid by DCP participants
  - Cost to employer community is unknown
- Possible federal legislation
  - Secure Act 2.0

16

Questions?

WASHINGTON STATE
Department of
Retirement Systems

17

Appendix C

Agency Recommendation Summary

The Department of Retirement Systems (DRS) requests funding to add a Roth option to the state's Deferred Compensation (457) Program. The agency has received requests from members to implement such an option within the state's 457 Plan. Some individuals prefer to invest for retirement with contributions that have already been taxed, and a Roth 457 has higher contribution limits than a Roth IRA.

Fiscal Summary

Fiscal Summary *Dollars in Thousands*	Fiscal Years 2022	Fiscal Years 2023	Biennial 2021-23	Fiscal Years 2024	Fiscal Years 2025	Biennial 2023-25
Staffing						
FTEs	0.0	3.0	**1.5**	2.5	0.0	**1.25**
Operating Expenditures						
Fund 001 - 1	$0	$609	**$609**	$379	$0	**$379**
Total Expenditures	**$0**	**$609**	**$609**	**$379**	**$0**	**$379**

Decision Package Description

What is the problem, opportunity or priority you are addressing with the request?

Members would like the opportunity to save for retirement using a Roth option, which essentially means that their contributions would be taxed as they're going into the fund, as opposed to when they're coming out of the fund. Although members can already contribute to a Roth IRA, separate from the state's system, contribution limits would be higher in a Roth 457.

What is your proposal?

DRS requests that funding be provided to enable DRS to implement a Roth option in the state's Deferred Compensation Program (a 457 Plan).

What are you purchasing and how does it solve the problem?

The decision package would provide funding to build a Roth option into the state's DCP over a period of 18 months. The funding package buys:

- FTEs, as outlined in the table under Workforce Assumptions, to implement the Roth program.
- Contracted record keeper services.
- Contracted programmers to augment existing DRS systems.
- Contracted management consulting with retirement expertise to support the agency in implementing the solution.

What alternatives did you explore and why was this option chosen?

The alternatives looked at different ways to fund an implementation project. The three alternatives explored were: 1) seek state funding to put the Roth in place, 2) increase the fee paid by all participants for administration of DCP or 3) establish a unique admin fee to be paid by only those members who choose to participate in the Roth.

The first option is recommended because of the impact of a fee increase relative to the low participation rates seen in other retirement systems who offer Roth options. The second option would represent a significant increase in the administrative fee paid by all participants during implementation while studies have identified that participation would only be around 10 percent. The fee required by the third option would be very difficult to calculate because it would depend not only on the number of active members who decide to start contributing to a Roth but also how many active and terminated members decide to convert existing assets to a Roth. Without a large asset base quickly shifting to the Roth option, recovering implementation costs would either require a significant short term fee increase or assessment of the fee over a period of years.

Assumptions and Calculations

Expansion, Reduction, Elimination or Alteration of a current program or service:

Adding a Roth option to the state's DCP would expand the existing program by giving DCP members a post-tax option to defer compensation into additional retirement savings.

It is important to keep in mind that adding a Roth option is not the same as adding a new investment choice, as how retirement funds are taxed is different than how retirement funds are invested.

Budget authority for DCP in the 2021-23 Biennium is $2,300,000 in FY 1 and $2,301,000 in FY 2. The estimated cost of the 18-month project would represent a 29% increase in the cost of the program over the duration of the project.

Detailed Assumptions and Calculations:

Administrative Assumptions

To develop this decision package, DRS made the following administrative assumptions for the implementation of the Roth option:

- DRS will need to create a new/separate plan in multiple DRS automated systems for managing Roth reporting and dollars.
- Roth will need to be set up with our existing record keeper for DCP, which will require them to make system changes, develop business requirements and conduct testing with DRS.
- WACs for DCP will need to be updated.
- DRS will need to update business procedures for internal operations (e.g., Trust Accounting, Accounts Receivable, and Retirement Services) to address new requirements.
- Roth contributions will be combined with existing pre-tax contributions for the calculation of the existing annual maximum for 457 plans.
- DRS will limit automatic enrollment default contributions to pre-tax dollars only, with an in-plan rollover option available to customers afterwards.
- Employers will be able to use the same Report Group to report Roth contributions as they use to report pre-tax contributions in DCP.
- Employer training materials will need to be updated to include Roth instructions and employer training webinars will need to be developed and training facilitated.
- DCP plan materials for members will need to be updated to include Roth information.
- Letters will need to be mailed to existing DCP customers by the Record Keeper, notifying them of the new Roth option.
- DRS anticipates an increased workload for approximately one year to support new enrollments and rollovers.

Note: Public employers who participate in the state's DCP may need to make changes to their own payroll system(s). DRS is not able to estimate that cost so it is not included in this decision package.

Calculation Assumptions

The salaries and benefits for all proposed FTEs are provided in the workload assumptions below, while management consultation and contracted programmers are both based on contracts we currently have in place for comparable services.

Workforce Assumptions:

Job Classification	Annual Amts Salary	Benefits	FY 2022	FY 2023	FTEs: 2021-23	2023-25	2025-27
Retirement Specialist 3	$61,224	$24,246		0.15	**0.1**	0.04	0.0
Mgmt Analyst 5	$88,644	$29,241		0.20	**0.1**	0.05	0.0
IT Busn Analyst-Jrny	$96,888	$30,744		1.00	**0.5**	0.25	0.0
IT Proj Mgr - Mgr	$123,636	$35,617		1.00	**0.5**	0.25	0.0
Comm Consult 5	$84,396	$28,469		0.13	**0.1**	0.03	0.0
IT Applications Developer-Senior	$112,167	$33,731		0.29	**0.1**	0.06	0.0
Rules Coordinator	$86,944	$29,090		0.05	**0.0**	0.00	0.0
Fiscal Analyst 2	$54,108	$22,949		0.05	**0.0**	0.01	0.0
Fiscal Analyst 5	$78,408	$27,377		0.15	**0.1**	0.04	0.0
Office Assistant	$42,428	$20,899		-	**-**	0.50	0.0
Total FTE's			**0.0**	**3.0**	**1.5**	**1.2**	**0.0**

How is your proposal impacting equity in the state?

The proposed option would be available to all public employees who work for employers that participate in the state's DCP. Additionally, funding the project out of the State General Fund would eliminate the cost to members who may never choose to participate in the Roth option. Studies have identified that although numerous 457 plans currently offer Roth options, only around 10 percent of members participate.

Strategic and Performance Outcomes

Strategic Framework:

This package supports DRS' strategic plan as it represents the addition of a retirement savings option requested by members.

Performance Measures	Incremental Changes 2022	Incremental Changes 2023	Incremental Changes 2024	Incremental Changes 2025
000622 - Number of new deferred compensation participants	0	0	0	0

Performance Outcomes:

Implementation of a Roth option may increase the number of new participants in the state's DCP although it is anticipated that a number of the eventual members in the Roth will be existing participants who change from pre-tax to post-tax contributions.

Other Collateral Connections

Puget Sound Recovery:

N/A

State Workforce Impacts:

N/A

Intergovernmental:

N/A

Legal or Administrative Mandates:

N/A

Stakeholder Response:

Implementation of a Roth option would respond to member requests from a small population as well as comments from local government employers.

Changes from Current Law:

N/A

State Facilities Impacts:

N/A

IT Addendum

Does this Decision Package include funding for any IT-related costs, including hardware, software, (including cloud-based services), contracts or IT staff?

No

Objects of Expenditure

Objects of Expenditure *Dollars in Thousands*	**Fiscal Years**		**Biennial**	**Fiscal Years**		**Biennial**
	2022	**2023**	**2021-23**	**2024**	**2025**	**2023-25**
Obj. A	$0	$309	**$309**	$191	$0	**$191**
Obj. B	$0	$91	**$91**	$67	$0	**$67**
Obj. C	$0	$209	**$209**	$121	$0	**$121**
Obj. E	$0	$0	**$0**	$0	$0	**$0**

Agency Contact Information

Mark Feldhausen
(360) 664-7194
mark.feldhausen@drs.wa.gov

LEOFF
Plan 2 Retirement Board

Roth 457/Deferred Compensation Option

Comprehensive Report
November 17, 2021

Issue

LEOFF 2 members requested a Roth 457 Plan option in the State's Deferred Compensation Plan

What is a Roth 457 Plan?

- 457 Plans may allow for deferrals to be made after taxes have been paid
- These after-tax contributions are call “Roth” contributions
- Roth contributions to a 457 Plan, along with investment returns on those contributions, are not taxed when a member withdraws them from the plan
- The earnings from Roth contributions not being taxed is a particularly significant benefit to younger members enrolled in DCP, whose contributions would accumulate earnings tax free for a longer time

Why is a Roth option not currently available?

- DRS is the plan administrator for DCP, and has the authority to implement a Roth option for DCP without legislation
- In January 2014, LEOFF 2 Board sent a letter to DRS requesting that they offer a Roth option for DCP
- Since 2014, DRS presented to the LEOFF 2 Board multiple times their intent to implement a Roth option for DCP
- In 2021 DRS informed the Board they were no longer prioritizing resources to implement a Roth 457 Plan option at this time

Update since June Board Meeting

- In July, the SCPP received a briefing from DRS that identified more detail regarding why they were not planning on implementing a Roth 457 option:
  - Previous related implementations of higher priority
  - Generally low take up rates for Roth options
  - Added complexity for both employers and customers
  - Cost/Effort of implementation
  - Possible federal legislation

DRS Budget Proposal

- In September, DRS filed a Budget Proposal with the Governor's Office to implement a Roth 457 option
  - Budget request is for General Fund money, meaning no admin fee increase to members
  - $609k in 2021-23 and $379k in 2023-2025
  - Governor's Budget scheduled to be released December 21

LEOFF 2 Employer/Member DCP Data

- Local employers must opt into the State's DCP program
- 67% (354) LEOFF 2 employers are enrolled
- 40% of LEOFF 2 members at these 354 employers are enrolled
- DRS estimates approximately 12% (423 LEOFF 2 members) of LEOFF 2 members enrolled in DCP will use the Roth option

Policy Options

- Option 1: No action at this time
- Option 2: Endorse legislation

Next Steps

- No action necessary at today's meeting
- Final briefing at the December 15th Board meeting

Thank You

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LEOFF

Plan 2 Retirement Board

Economic Assumptions Adoption

November 17, 2021

Issue

- The Board is tasked with adopting economic assumptions every 2 years
  - Any changes subject to revision by the Legislature
- No change to economic assumptions in 2019
- The last adopted changes to economic assumptions occurred in 2017
  - Inflation 3.00% to 2.75% (0.25%)
  - Salary Growth 3.75% to 3.50% (0.25%)
  - Annual Investment Return 7.50% to 7.40% (0.10%)

Economic Assumptions Change Recommendations

Assumption	Current	Recommended
Inflation	2.75%	2.75%
General Salary Growth	3.50%	3.25%
Assumed Investment Return	7.40%	7.00%

Options

1. Adopt all the recommended assumption changes

2. Adopt only recommended assumed investment return change

3. Do not adopt assumptions changes

Impacts of Change to All Assumptions

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

Note: Preliminary values subject to change. Actual results may also vary from these preliminary values. Baseline Projection under current assumptions and returns

Change in Total Employer Projected Contribution Rates—Preliminary			
	2021-23 Biennium	2023-25 Biennium	2025-27 Biennium
Baseline Projection	**8.53%**	**8.53%**	**7.74%***
90% Minimum rate		7.71%	7.74%
100% Minimum rate		8.57%	8.60%
New Projected Rate	**8.53%**	**8.53%**	**8.30%***
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.*

Impact of Change to Only Investment Return

Change in Funded Ratio (FR)–Preliminary				
	As of June 30, 2019	As of June 30, 2021	As of June 30, 2023	As of June 30, 2025
Baseline Projection	**111%**	**113%**	**113%**	**113%**
FY 2021 Return (a)	0%	3%	10%	17%
7% Interest Rate Assumption (b)	-6%	-7%	-8%	-9%
Total Change (a + b)	**-6%**	**-4%**	**2%**	**8%**
New Projected FR	**105%**	**109%**	**116%**	**121%**

Note: Totals may not agree due to rounding. 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.

Potential Changes to Economi...

Change in Total Employer Projected Contribution Rates—Preliminary			
	2021-23 Biennium	2023-25 Biennium	2025-27 Biennium
Baseline Projection	**8.53%**	**8.53%**	**7.74%***
90% Minimum rate		7.71%	7.74%
100% Minimum rate		8.57%	8.60%
New Projected Rate**	**8.53%**	**8.53%**	**8.56%***
90% Minimum rate		8.52%	8.56%
100% Minimum rate		9.47%	9.51%

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 7% investment rate of return assumption.

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

*** Excludes OSA's recommended change in General Salary Growth assumption.*

Questions?

Steve Nelsen

Executive Director

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360-586-2323

2022 Board Meetings

LEOFF
Plan 2 Retirement Board

January

S	M	T	W	T	F	S
						1
2	3	4	5	6	7	8
9	10	11	12	13	14	15
16	17	18	19	20	21	22
23	24	25	26	27	28	29
30	31					

February

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27	28					

March

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27	28	29	30	31		

April

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24	25	26	27	28	29	30

May

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22	23	24	25	26	27	28
29	30	31				

June

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26	27	28	29	30		

July

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31						

August

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September

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October

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November

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December

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18	19	20	21	22	23	24
25	26	27	28	29	30	31

MEETING LOCATION: Meetings will be held virtually until further notice
CONTACT: Phone: 360.586.2320 Recep@leoff.wa.gov

Meeting Dates

State Holidays

LEOFF
Plan 2 Retirement Board

2022 STAKEHOLDER EVENTS AND CONFERENCES

STATE HOLIDAYS	LEOFF 2 BOARD
WSCFF	WACOPS
IFEBP	NCPERS

January

S	M	T	W	T	F	S
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2	3	4	5	6	7	8
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February

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27	28					

March

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April

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24	25	26	27	28	29	30

May

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15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30	31				

June

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5	6	7	8	9	10	11
12	13	14	15	16	17	18
19	20	21	22	23	24	25
26	27	28	29	30		

July

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3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28	29	30
31						

August

S	M	T	W	T	F	S
	1	2	3	4	5	6
7	8	9	10	11	12	13
14	15	16	17	18	19	20
21	22	23	24	25	26	27
28	29	30	31			

September

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4	5	6	7	8	9	10
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18	19	20	21	22	23	24
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27	28	29	30			

December

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				1	2	3
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18	19	20	21	22	23	24
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