



OSA Recommendation on Economic Assumptions

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Today's Presentation

- Highlights of our two reports
 - Financial condition
 - Long-term economic assumptions
- State actuary's perspective on the financial condition and recommended study



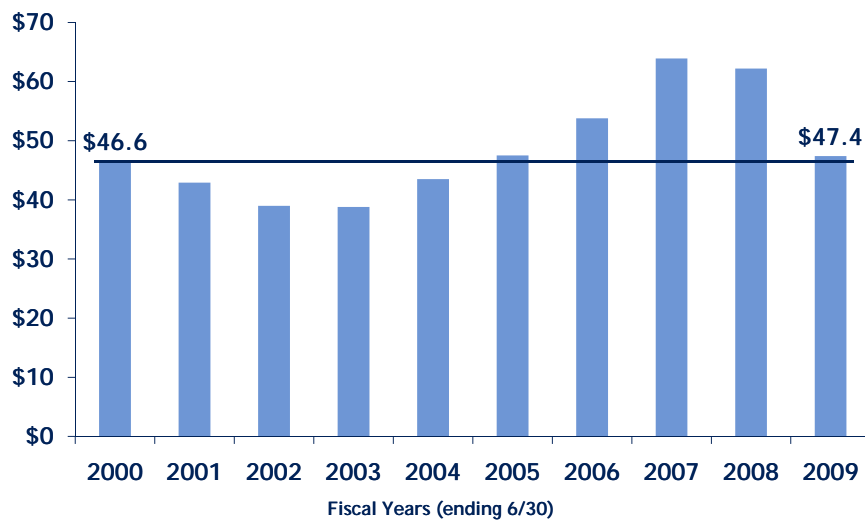
Focus On Financial Condition

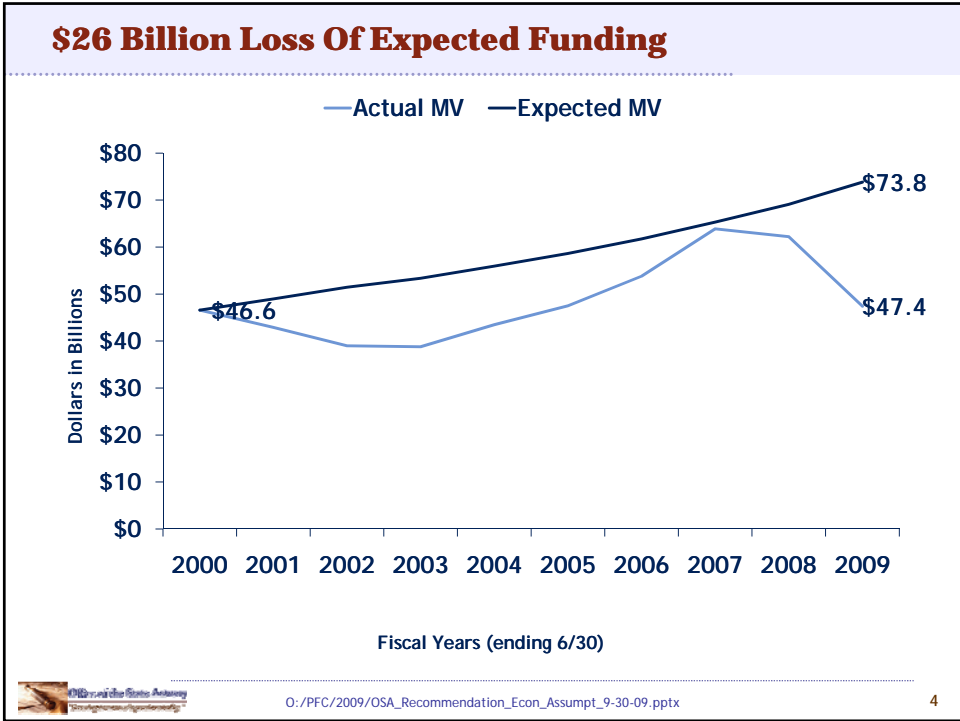
- Systems face significant short- to medium-term funding challenges
- Business as usual not likely to see them through
- Meeting the challenges will require coordinated action and further study



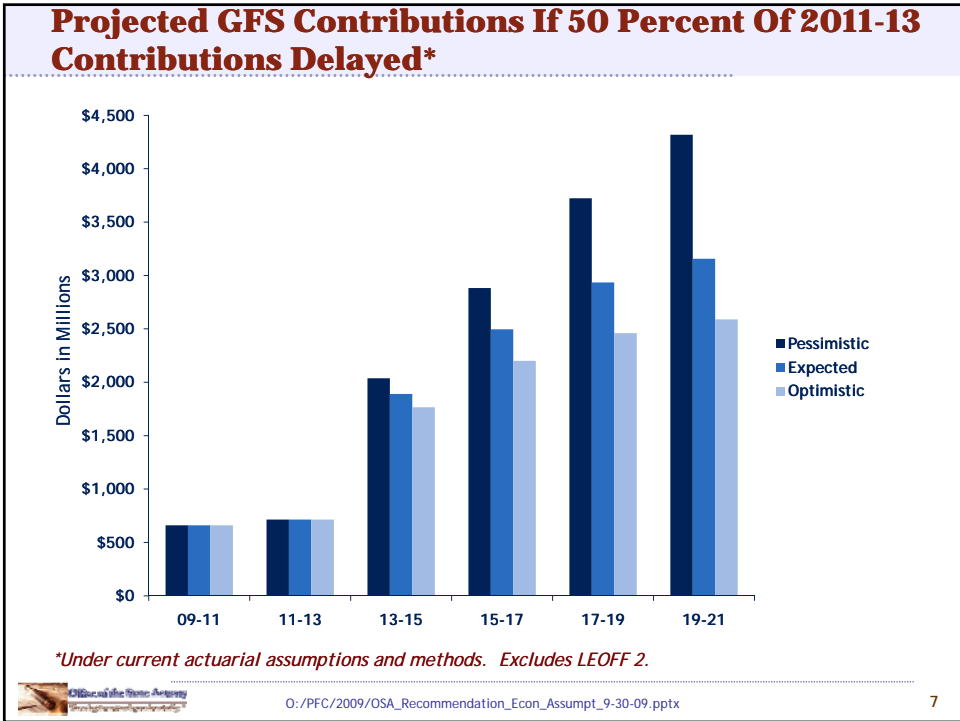
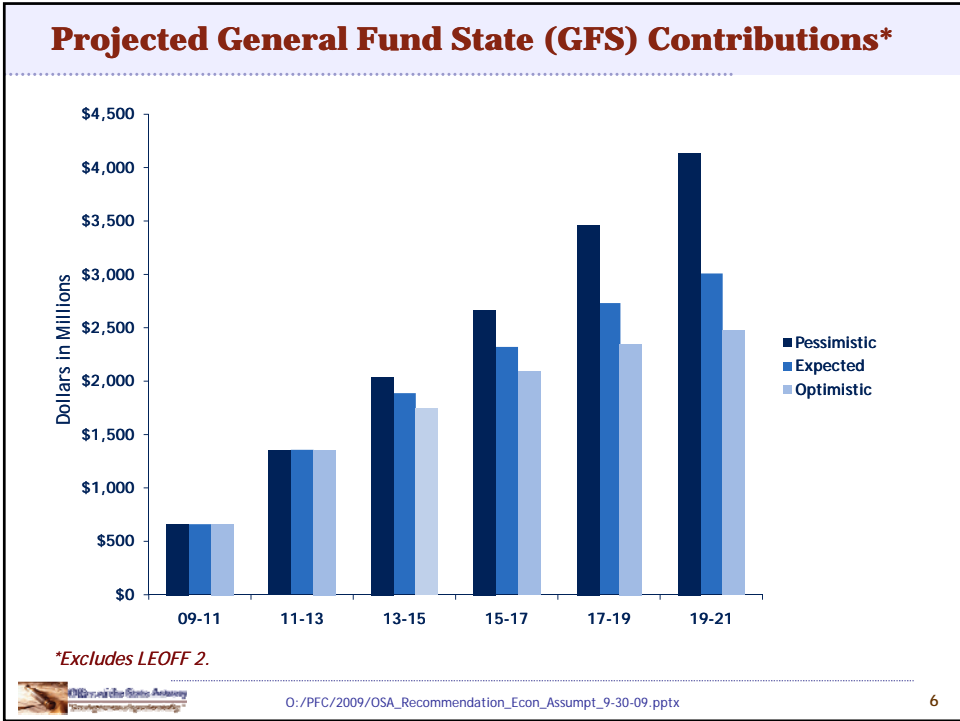
A Lost Decade of Funding Progress

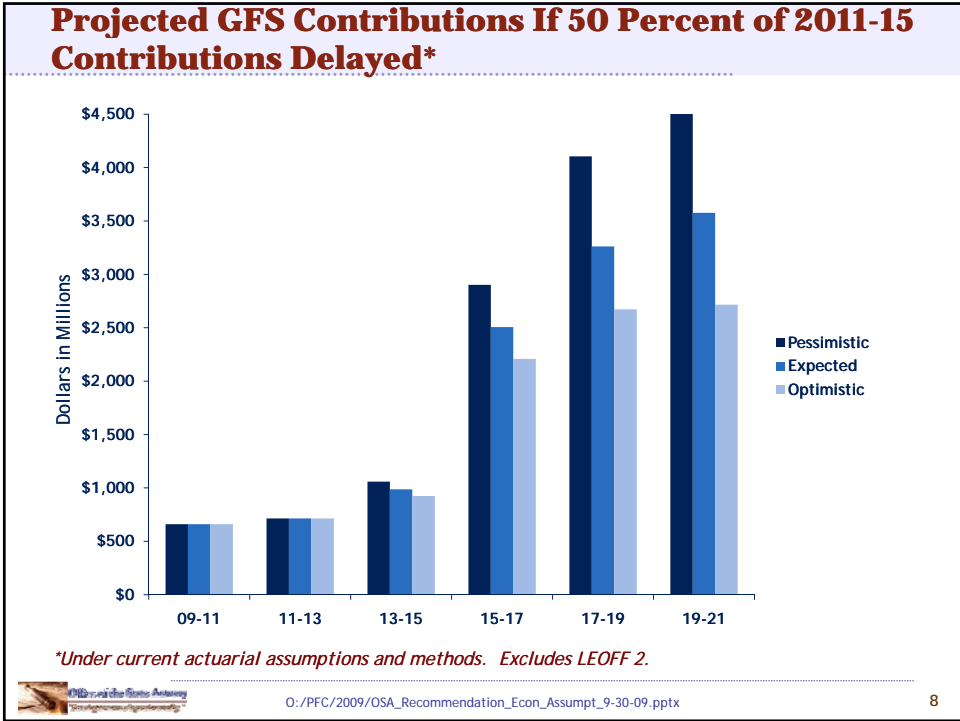
Historical Market Value of Assets (Billions)

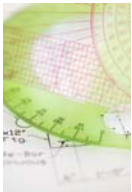




- ### Steep Increases In Future Contributions Expected
- Loss in funding will emerge over the next ten years
 - Due to asset smoothing method
 - Recovery of lost funding will require steep increases in future contributions
 - Future investment returns unlikely to prevent increase in contributions
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- ### Long-Term Economic Assumptions
- Current assumptions are reasonable but not our best estimates
 - Adopting OSA's recommended assumptions improves the long-term health of plans
 - Makes short- to medium-term funding challenges worse
 - Recommend coordinating changes to economic assumptions with a plan to manage funding challenges
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Concluding Thoughts On Financial Condition

- Retirement systems face significant short- to medium-term funding challenges
- Steep increases in future contributions required
- Funding delay will increase upward pressure on future contribution requirements
- Plans 2/3 remain healthy, but PERS 1 and TRS 1 at-risk of running out of assets prematurely
- Plan health will weaken if employers can't make contributions
- Coordinated action and further study recommended



Check-In

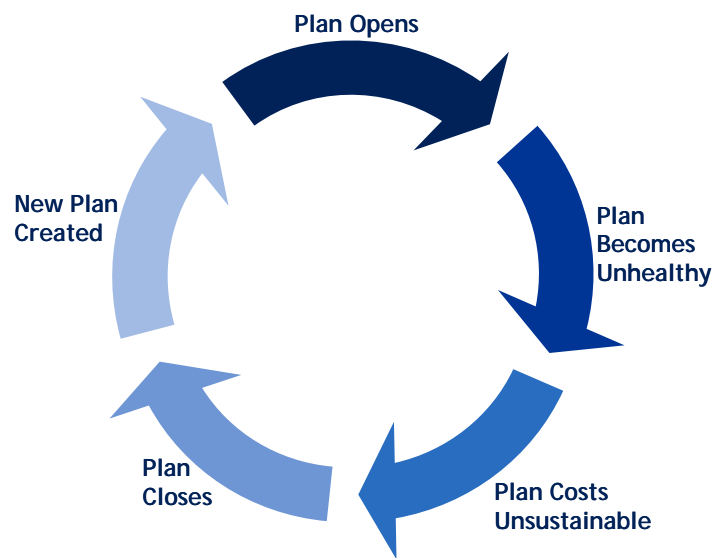
- What's been covered so far?
 - Highlights of reports on financial condition and long-term economic assumptions
 - Recommended economic assumptions
- What's next in this presentation?
 - Another perspective on financial condition
 - Recommended process to address financial condition



Understanding The Public Pension Life Cycle

- Pension systems go through certain stages in their life
- Stages have different implications for budgets
- Understanding and managing this life cycle improves future plan health and lessens budget risks

Public Pension Life Cycle



Pension Life Cycle In Washington

- Plans 1
 - Opened in 1930s and 1940s
 - Unfunded liability added with benefit improvements over time
 - Funding shortfalls created additional unfunded liability
 - Costs became unsustainable
 - Plans closed
 - Plans 2/3 created



Lessons Learned From Plans 1

- Avoid unfunded liability
- Avoid benefit improvements you can't fund over members' working careers
- Make regular and systematic contributions

Where Are We In The Plans 2/3 Life Cycle Today?

- Thirty-two years later we see similarities to Plan 1 life cycle
- Health beginning to deteriorate
- Additional contributions required to stabilize health
- Risk of unsustainable costs, especially when combined with Plan 1 costs



Convergence Of Life Cycles

- PERS 1 and TRS 1
 - Closed since 1977, but significant legacy costs remain
- Plans 2/3
 - Open since 1977 and healthy today, but significant contributions required to prevent repeat of Plan 1 life cycle



Opportunity To Address Challenges

- Break from past practices
- Shift in focus to identifying, measuring, and managing retirement system risks
- Recommendation
 - Perform risk analysis with risk measures



Can We Sustain Our Current Plans?

- Not an easy question to answer
- Risk analysis and risk measures can help
- Coordinate revenue forecast with actuarial simulations for required contributions (pension costs)
- Compare projected pension costs to projected available revenue
 - Over a long-time horizon
- Determine chance pension costs will exceed available revenue and by how much



What If We Can't Sustain Our Current Plans?

- No easy solutions
- Lower benefits for new hires?
 - How do you determine the level of benefits for future new entrants?
 - How do you plan for the legacy costs of Plan 1 and avoid creating legacy costs for the Plans 2/3?
- Increase "available revenue?"
 - How much and how long?
- Risk analysis can help



Avoiding Repeating Life Cycles

- Once you're on the road of sustainability, how can you stay the course?
- Review plan history and identify the risk factors that lead to unsustainable costs
 - For example, funding/contribution shortfalls, retroactive benefit improvements, investment losses, contribution rate volatility, etc.
- Set measures for each risk factor - risk measures
- Analyze and monitor risk factors - risk management
- Create new decision making tools for pensions



The Goal

- Improve the health of the state's retirement systems
- Ensure long term sustainability
- Develop tools to better understand impacts of funding and policy decisions on future budgets
- Institutionalize the solution
- Avoid a repeating pension life cycle
- Create shared ownership in the solution

