

SENATE BILL REPORT

SB 5494

As of February 10, 2011

Title: An act relating to changing the default investment option for new members of the defined contribution portion of the plan 3 retirement systems.

Brief Description: Addressing the default investment option available to new members of the plan 3 retirement systems.

Sponsors: Senators Brown, Zarelli and Shin.

Brief History:

Committee Activity: Ways & Means: 2/03/11.

SENATE COMMITTEE ON WAYS & MEANS

Staff: Erik Sund (786-7454)

Background: The Public Employees' Retirement System Plans 2 and 3 (PERS 2/3) provide benefits for all regularly compensated public employees and appointed and elected officials that first entered eligible positions since 1977, unless they fall under a specific exemption from membership, such as qualification for another of the state retirement systems. Covered employers include all state agencies and subdivisions and most local government employees not employed by the cities of Seattle, Tacoma, and Spokane. The Teachers' Retirement System and School Employees' Retirement Systems Plans 2 and 3 (TRS 2/3 and SERS 2/3) provide benefits for certificated and classified employees who first entered eligible positions with school districts, educational service districts, or certain other public educational employers after September 30, 1977.

PERS, TRS, and SERS Plan 2 are defined benefit plans that provide a retirement allowance based on 2 percent of final average salary for each year of service, and a normal retirement age of 65. Early retirement benefits are available beginning at age 55, with reductions depending on the members age and years of service. Contributions for the plan vary from year to year with actuarial requirements, are divided equally between employers and employees, and are each paid into the defined benefit pension fund for purposes of supporting the defined benefits at retirement.

PERS, TRS, and SERS Plan 3 are hybrid defined benefit/defined contribution retirement plans. Employer contributions support a 1 percent of final average salary benefit for each

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year of service with a normal retirement age of 65. Early retirement benefits are similar to those offered in Plan 2. Member contributions are made to an individual defined contribution account. A member's contribution rate option, which may result in a contribution rate as low as 5 percent or as high as 15 percent, is selected by the employee at the time of employment and is fixed for the duration of the employment relationship.

There are a variety of investment options available to Plan 3 members . The default selection for members who do not select another option is the State Investment Board's Total Allocation Portfolio (TAP) which is invested along with the funds of the defined benefit plans. The TAP is invested with the goal of earning the maximum possible rate of return achievable over the long-run at a prudent level of investment risk. Another investment option available to Plan 3 members is a Retirement Strategy fund. Retirement Strategy funds are diversified portfolios that are managed with a target retirement date in mind, investing more aggressively early on and then gradually adjusting to a more stable mix of investments as the target date approaches.

Summary of Bill: The default investment option for the defined contribution account of a member of PERS 3, TRS 3, or SERS 3 who does not select an investment option is changed from the State Investment Board's Total Asset Portfolio to the Retirement Strategy Fund with the target date closest to the retirement target date of the member.

Appropriation: None.

Fiscal Note: Available.

Committee/Commission/Task Force Created: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: About 20-25 percent of Plan 3 members fail to choose an investment option at the time they become members. Additionally, members who don't make an investment choice at first tend not to make adjustments to their investment allocations later on. The Total Allocation Portfolio is a good performer but is perhaps too volatile for the savings of individuals nearing retirement. The Washington Federation of State Employees appreciates the efforts of the State Investment Board to take better care of employees in Plan 3 who don't choose an investment option, however we still believe that enrollment in Plan 2 is the best default option.

Persons Testifying: PRO: Pat McElligott, Theresa Whitmarsh, Washington State Investment Board; Matt Zuvich, Washington Federation of State Employees.